REPORT TO THE

SAN FRANCISCO BOARD OF SUPERVISORS

MANAGEMENT AUDIT

OF THE

TAX COLLECTOR'S OFFICE

BOARD OF SUPERVISORS
BUDGET ANALYST

APRIL, 1995

CITY AND COUNTY  OF SAN FRANCISCO

BOARD OF SUPERVISORS

BUDGET ANALYST

1390 Market Street, Suite 1025, San Francisco, CA 94102 (415)554-7642

April 25, 1995

Honorable Tom Hsieh
and Members of the Board of Supervisors
City and County of San Francisco
Room 410, Veterans Building
401 Van Ness Avenue
San Francisco, CA 94102

Dear Supervisor Hsieh and Members of the Board of Supervisors:

Transmitted herewith is the Budget Analyst's management audit report concerning the San Francisco Tax Collector's Office.

This management audit report contains eleven findings and 81 recommendations. Full implementation of the recommendations contained in this management audit would decrease the Tax Collector's overall costs and increase revenues by a net amount of approximately $7.1 million to $16 million annually for the City. Depending on future legal opinions of the City Attorney and policy decisions of the Board of Supervisors, the City could realize an additional $3.5 million to $6.9 million of one-time payments as a result of delinquent Business Taxes and Registration Fees owed to the City by taxicab companies or its drivers. Implementation of the recommendations contained in our report would require an additional estimated one-time net cost of $215,426.

These estimated savings which we have identified do not include a conservative estimate of an additional $14.3 million annually from Payroll and Gross Receipts Taxes owed to the City. The taxes are owed to the City because an estimated 9,376 to 53,376 businesses are not registered with the Tax Collector's Office and therefore do not pay taxes.

Furthermore, because of the limited data available, the savings to be realized from many of our recommendations could not be quantified, although implementation of such recommendations (such as an expedited Business Tax delinquent

collections process) should result in significant additional savings to the City, including increased revenues, reduced costs and enhanced efficiencies.

All of the revenue increases resulting from our recommendations would result in additional General Fund monies to the City, except for $294,145 in estimated annual dog license fees which would accrue to the Animal Welfare Fund and other license fees and Rent Board fees of an estimated $371,805 annually which would accrue to the Department of Public Works and the Rent Board.

The Tax Collector's written response to our report is attached, beginning on page 167. The Budget Analyst has annotated the Tax Collector's response indicating additional comments where the Budget Analyst believed it was necessary to respond to the Tax Collector's written response. These additional comments of the Budget Analyst follow the Tax Collector's response.

While the written response of the Tax Collector indicates that he either fully or partially concurs with ten of our eleven findings included in this report, there are several areas of strong disagreement. In his written response, the Tax Collector states that "the projection of 53,000 unregistered businesses is perhaps somewhat overstated" because "the sampling method employed was neither statistically random nor sufficiently large to be representative." Since it is impossible to conduct a statistically valid sample of an unknown population (in fact, the Tax Collector himself does not know the actual total number of businesses in San Francisco), the Budget Analyst acknowledged that such a sample could not be taken. The fact that no accurate list of the population of San Francisco businesses exists is exactly the problem addressed in this section of our report. The Budget Analyst, however, did use three different measures in an attempt to accurately estimate the number of unregistered businesses in San Francisco.

The Budget Analyst attempted to be fair in our selection of sites in that we did not select (1) outlying neighborhoods of the City, (2) at-home businesses or (3) any businesses that are not located in the City but do business in San Francisco, since we concur that such businesses would have a very low business registration compliance rate. Rather, the Budget Analyst endeavored to sample five different commercial buildings, including retail, office, manufacturing and service industries located in a variety of locations: one large complex in China Basin, three sites South of Market on Third Street and one central downtown location at Pine and Montgomery Streets. The Budget Analyst made personal site visits to each location, using the directory on the ground floor and then worked with the Tax Collector's Office, which obtained listings from the lessors of each of the same buildings. Based on such data, which has been fully corroborated by the Tax Collector's staff, of the 359 businesses selected, 43 percent or 153 of the 359 businesses were not registered by the Tax Collector.

This 43 percent rate of unregistered businesses may, in fact, be understated. That is because the Budget Analyst omitted the many unregistered firms that were taken from the building directories but not contained on the lessor's list of

building tenants obtained by the Tax Collector's Office. For example, based on a follow-up telephone survey at the 369 Pine Street location, wherein many of the tenants were subleasing space and thus did not appear on the lessor's list, the Budget Analyst conservatively estimates that 63 percent of the businesses at this one downtown location were not registered with the Tax Collector's Office. This reexamination of the data also identified serious flaws in the methodology of the lessor's list used by the Tax Collector's Office to identify unregistered businesses.

In his response, the Tax Collector includes the State's Employment Development Department (EDD) report of a total of 27,500 Employer Files in San Francisco as an indicator of the total number of businesses in San Francisco, while simultaneously indicating that the Tax Collector has 64,951 businesses currently identified by the Tax Collector's Business Tax computer system. This EDD estimate grossly understates the number of businesses in San Francisco, since EDD only retains records of businesses with employees, but not individual proprietors. The fact that the Tax Collector has included this obvious underestimate, which lists less than one-half as many businesses as the number actually registered by the Tax Collector, causes the Budget Analyst to question whether the Tax Collector intends to represent or understate the actual number of businesses in San Francisco in his response.

In his response, the Tax Collector indicated that his office conducted a "random survey of three downtown buildings (One Embarcadero Center, Two Embarcadero Center and 525 Market Street), which may be slightly more representative than the Budget Analyst's sample." The Tax Collector reportedly found a 93.75% rate of registration compliance. The Budget Analyst seriously questions this "random survey" of three major downtown office buildings. The Tax Collector selected only businesses in San Francisco's financial district, where businesses are likely to be more stable and larger, and the types of businesses are limited. Nevertheless, the fact is that the Budget Analyst's sample of five different buildings documented that 43 percent of the building tenants were not registered by the Tax Collector and the Tax Collector concurred with the results of the data collected by the Budget Analyst.

SUMMARY OF FINDINGS AND RECOMMENDATIONS

The following paragraphs present a summary of our management audit findings and recommendations.

Section I.1: Accounting and Statements

Accounting and data entry functions are currently distributed throughout the Divisions of the Tax Collector's Office. Efficiency improvements that will improve collections can best be implemented by establishing a consolidated Accounting Division, as recommended by the Tax Collector's Total Quality Management (TQM) Task Force Charlie.

Current collections efforts are also hampered by the nearly four-month process of entering Business Tax Statements to the BTS system, which will likely be shortened by the planned introduction of scanners for statement entry. A consolidated Accounting Division would provide an environment in which performance goals for statement entry could be monitored and enforced.

In addition, the current fragmented check control process takes time away from revenue producing activities. Business Tax, License, Fees and Unsecured Personal Property Tax (UPP) check control should be centralized, after the centralization of accounting is complete. Transferring check control activities from revenue producing Auditors and Investigators would result in an estimated $276,641 annually in increased collections for the City.

Tracking of delinquent accounts can also be improved in several ways. Use of the BTS system should be maximized to facilitate calculation of interest and penalties, eliminating manual calculation by multiple Divisions. The proposed Accounting Division should cross-check delinquent UPP and Business Tax Accounts, so that taxpayers can be notified of both delinquencies simultaneously, and Collections Officers can more efficiently pursue full payment.

The Assessor's Office is responsible for substantial delays in posting reassessments in property values to the Tax Rolls. As a result, the Tax Collector has to process numerous check returns and subsequent refunds, as taxpayers submit initial payments for reassessed amounts that cannot be accepted by the Tax Collector until they are reflected on the Tax Rolls. The Tax Collector should closely monitor and support the progress of automation efforts in the Assessor's Office.

In general, consolidating the Department's accounting and check control activities and implementing the efficiency improvements recommended in this Section would result in an estimated $276,641 annually in increased collections, improve overall collections activities and increase revenues by permitting earlier notification of delinquent taxpayers, while providing collections staff with more complete and accurate information about total taxpayer liabilities.

Section I.2: Automation

The Tax Collector has invested more than $3.75 million in new automated systems for maintaining taxpayer account data over the past three years. This investment is largely going to waste, because staff have not been trained to take advantage of the improvements. Available training is too brief, too narrow in scope and provides no follow-up to ensure that staff are able to use the systems they need at maximum efficiency. The Tax Collector should enhance training, and then require managers to evaluate staff's mastery of systems related to their jobs.

The Administration Division should convene and consult with internal user's groups to provide end-users with on-going information about the custom software developed by the Controller's Office for the Tax Collector's Office. The Division should provide clear procedures for communication of decisions related to the automated systems to end-users in the Department.

The Tax Collector's Office has restricted access for individual staff to the existing computer systems based on position duties. Many of the restrictions serve no useful security purpose, yet prohibit staff from accomplishing tasks without assistance from other staff. The access restrictions also keep staff ignorant of how their work affects others. Such access rules should be revised to provide at least read-only access to improve efficiency.

The Tax Collector should also work towards linking the Business Tax System (BTS) with the Unsecured Personal Property Tax System (UPP), the database maintained by the Assessor, and the City's main financial accounting system, notwithstanding budgetary considerations and ordinance changes that might stress the Tax Collector's resources. Establishment of working system interfaces will improve collections, facilitate identification of unregistered businesses, and simplify taxpayer assistance.

The benefits of improving automation training, establishing automation user's groups, improving access to databases and evaluating staff's mastery of automated systems will be significant long-term productivity gains and improved ability to collect revenues due the City.

Section I.3: Taxpayer Assistance

The Tax Collector's Office provides assistance to taxpayers separately in the Property Tax, Business Tax and Licensing Divisions. However, most of the taxpayer assistance staffing is provided by rotating staff who perform other functions within their respective Divisions. Problems include inadequate staffing of telephones, excessive transfers of taxpayers from division to division within the Tax Collector's Office, provision of incorrect information, long lines and communication problems due to language differences.

The Tax Collector is taking constructive steps to remedy these problems through a Single Point of Contact (SPOC) desk to direct taxpayers to the correct division, as well as through a Total Quality Management (TQM) task force ("Task Force Bravo"), which issued a report on taxpayer assistance in October of 1994 recommending the establishment of a consolidated taxpayer assistance group. Task Force Bravo also recommended that the Service Representatives staffing taxpayer assistance receive telephone and customer service training, that networks between computer systems carrying tax data be established, and that InfoCal stations and self-service VCRs with multi-language video instructions be provided in the taxpayer assistance area. We endorse the Task Force recommendations.

Several of the recommendations presented in other sections of this management audit will, if implemented, help provide the proposed Service Representatives with quick access to accurate information, including: (1) providing employees with access to all computer screens they might need and training in what all systems can provide; (2) creation of a centralized Accounting Unit; (3) consolidation of license fee billing with Business Registration and Property Tax bills; and (4) providing more realistic tax determinations to delinquent business taxpayers. Progress in improving taxpayer assistance should be monitored through user surveys and evaluation of service quality in the Tax Collector's Annual Report.

It is impossible to measure the revenue effects of qualitative changes in the delivery of taxpayer assistance. However, it is reasonable to conclude that providing more efficient, accurate taxpayer assistance will increase voluntary compliance with tax regulations, thereby increasing revenues. The estimated cost of providing two work stations with videotaped instruction translated into selected languages would cost up to $92,000 in one-time expenses.

Section II.1: Licensing

The License Division prepares and mails a separate bill for each license, even if an individual or business owes more than one license fee. Also, the property tax bill and the business registration bill are prepared and mailed separately from licenses, so that most individuals and businesses receive more than one bill from the Tax Collector each year. The Tax Collector should issue a consolidated property tax bill, including property taxes, the Rent Stabilization and Arbitration fee, and all four DPW fees. The Tax Collector should also issue a consolidated business registration bill, including the business registration fee, all Fire Department and DPH fees, and most Police Department fees. The Business Tax Division should allocate resources to administering license fees for individuals.

Our recommended reallocation of licensing responsibilities will result in improved customer service, increased efficiencies and reduced administrative costs. The recommendations would result in one-time costs for computer programming of approximately $150,000, and on-going cost savings of $487,622.

Also, the Tax Collector can expect the collections rate for license fees to increase from 90.1 percent to 97.19 percent for DPW and for the Rent Board, and the City's business registration collection rate should improve. Such increased collections would have resulted in additional revenues of at least $371,805 in FY 1993-94. Based on staffing reductions and license fee revenues, the combined savings and increased revenues would therefore equal $859,427.

Section II.2: Dog Licenses

Currently, the Tax Collector's License Division estimates that there are 12,000 licensed dogs. Based on a total of approximately 177,000 San Francisco dogs, only 6.9 percent of the City's dog population is licensed. Neither the Department of Animal Care and Control nor the Tax Collector conduct an Animal Licensing Program that would identify pet owners and require them to license their animals. The Department of Animal Care and Control should assume responsibility for implementing an Animal Licensing Program, and the Tax Collector's Office should no longer bill individuals for dog license renewals.

San Francisco charges a license fee of $12 for unaltered dogs and $6 for altered dogs, while Bay Area jurisdictions charge an average of $19 and $9, respectively. The Department of Animal Care and Control should increase dog license fees commensurate with Bay Area jurisdictions.

Costs for administering dog licenses would increase from approximately $47,145 to an estimated $127,567 in the first year and up to $284,500 after five years. Dog license revenues would increase from $98,500 to $630,000. Net revenue is currently $51,355; under the proposed new program, net revenue would be $345,500, an increase of $294,145.

Section III.1: Business Tax Auditing

Audits are conducted of businesses that have not filed tax returns and/or have not registered with the City, when such unregistered/delinquent accounts should be pursued by a Collections Division. This practice cost the City $186,235 to $1,381,573 in uncollected revenue in FY 1993-94.

Audit productivity has declined substantially in the past three years, due to: (1) reduced accounting staff; (2) implementation of several legislative changes; (3) early retirements and long vacancies; and (4) coincidental implementation of the complex Business Tax System. Relieving auditors of taxpayer assistance ($470,924) and account maintenance ($1,177,311) duties would increase collected revenues from audited deficiencies by an estimated total of $1.6 million per year. The Business Tax Division has begun to implement this redirection of auditors to focus them on audit activities, and the decline began to reverse itself in FY 1993-94. Careful planning and budgeting for implementation of changes in tax regulations by the Tax Collector and the Board of Supervisors, and implementation of our recommendations for automation training and communications would also increase audit productivity. Development and enforcement of productivity standards to achieve an average of one audit completed weekly by each auditor would further increase collected revenues by an estimated $1 million.

Selection of which firms the Tax Collector audits has been carried out on an ad hoc basis, without careful prioritization. While the Business Tax Division is in the process of implementing an automated selection system, the Division needs to study historical data to refine selection criteria. The Business Tax Division should also improve internal controls in the areas of audit assignments and account servicing.

Revenue benefits from our recommendations, detailed above, would total an estimated $2.8 to $4 million annually. New staff costs, to be determined by the Tax Collector, would be incurred if the Chief Auditor's analysis of telephone taxpayer service activities by auditors shows that additional accounting staff should be hired to perform this function, so that auditors can focus on auditing activities. However, such costs would only be warranted if they are more than offset by additional audits being conducted, resulting in increased audit deficiency billings and collections.

Section III.2: Review of City Park Audit

Review of an audit conducted by the audit staff of the Business Tax Section of the Tax Collector's Office found that audit staff: (1) used methodology that is not supported by work papers, resulting in an audited deficiency billing that was $35,574 less than if the existing methodology developed by the City's Department of Public Works (DPW) had been used; and (2) neglected to assemble the complete working papers necessary to establish an audit trail and permit thorough supervision by senior staff auditors.

Although the Tax Collector billed and City Park has now paid the $94,884 of audited deficiencies and the associated penalties and interest, our recommendations direct the Tax Collector to bill City Park for the additional $35,574. Furthermore, we recommend that the Tax Collector develop more detailed audit procedural guides and in-house training for staff. This should result in improved audits of business taxpayers, which should lead to more accurate audit deficiency billings.

Section III.3: Business Registration

There is no unit of the Tax Collector's Office with clear responsibility for registering businesses. The Business Tax Division and the Investigations Division make limited attempts to identify businesses that need to register, but estimates of the number of unregistered firms doing business in San Francisco range from 9,000 to 53,000.

To estimate the portion of unregistered business in San Francisco, the Budget Analyst visited five commercial buildings. Based on the data collected and verified

by the Tax Collector's Office, of the 359 businesses surveyed, a total of 206 (57%) were registered with the Tax Collector and 153 (43%) were not registered. Unregistered businesses cost the City an estimated maximum of $6.8 million annually in business registration fees. Assuming that these unregistered businesses owe the average annual Gross Receipts and Payroll Taxes paid by businesses to the City, a conservatively estimated additional $14.3 million annually in such taxes would also be lost.

The Tax Collector should establish a Business Identification Unit in the Business Tax Division, with responsibility for identifying and registering businesses, staffed by an 1832 Management Analyst, at a cost of $75,000, including salary and fringe benefits. This Business Identification Unit should work with City Departments, the Chamber of Commerce and other branches of government to identify all businesses operating in San Francisco. We propose that the 1832 Management Analyst be a limited tenure position, to be eliminated if the Business Identification Unit fails to garner enough registration fees or business taxes to support its salary and benefits costs.
The Business Identification Unit should track all identified businesses to ensure that they actually register with the City. Those that may owe Payroll and Gross Receipts Taxes should be required to submit tax statements and payments. Only large, complex accounts with statements that appear to be inaccurate should be audited; the rest should be subject to the standard collection procedures recommended in Section IV.2.

Section III.4: Taxicab Driver Status

The Tax Collector has not provided guidelines regarding the classification of taxicab drivers. As a result, taxicab companies never include taxicab drivers' receipts as part of gross receipts or payroll costs in calculating businesses taxes owed, and taxicab drivers never register as independent contractor businesses. Therefore, the City does not receive any of such business tax revenues from taxicab companies or drivers.

The Tax Collector should immediately establish a checklist for determining the status of taxicab drivers as independent contractors versus employees and immediately begin collecting these revenues. Additional annual revenue of an estimated $702,750 to $1,376,700 would result from providing guidelines to taxicab companies and drivers regarding the employment status of taxicab drivers.

The City Attorney should determine whether the Tax Collector has the authority to collect retroactive registration fees and business taxes in this case. If so, the Board of Supervisors and the Tax Collector should make a policy decision regarding the retroactive collection of registration fees and business taxes. If the Tax Collector collects retroactive payments, additional one-time revenue of $3,513,750 to $6,883,500 for five years of retroactive payments could be collected.

Section IV.1: Delinquent Collections Process: Business Tax

Although the Tax Collector does not have information about total current delinquent taxes and fees owed to the City, as of June, 1994, the Tax Collector reported to the Budget Analyst that $144 million in Business (Gross Receipts and Payroll) Taxes was outstanding. This $144 million represents an intentionally inflated estimate, due to the Tax Collector's policy of estimating Business Taxes for businesses that do not file tax returns at 150 percent of the previous year's taxes.

Almost one-third (31 percent) of San Francisco businesses (18,000 to 19,000 per year of an estimated total of 60,000 businesses) do not file a Business Tax Statement with the Tax Collector's Office as required. For those businesses, the Tax Collector inflates the estimated outstanding Business and Payroll Tax in statements mailed to delinquent businesses, does not maintain records of taxpayer response, and uses these inflated estimates to estimate outstanding revenue. As a result, taxpayers are confused and alarmed, the Tax Collector's customer service staff resources are overtaxed, and the Tax Collector cannot evaluate the efficacy of the overstated estimates. Using a realistic estimate for assessing unpaid business taxes, including penalties and expediting the delinquent collection's process, should reduce taxpayer frustration, improve the taxpayer's incentives to respond, reduce the business tax delinquency rates and therefore increase overall revenues for the City.

In addition, the Tax Collector did not impose a $100 penalty against businesses for failing to file a Business Tax Statement, which resulted in lost revenue of $1.8 to $1.9 million in 1994. Based on the Tax Collector's current policy, the current $500 penalty would not be imposed for each violation incident. We recommend that a penalty fee of possibly $100 for each subsequent occurrence within a given year be imposed for each delinquent filing. Charging a $100 penalty against taxpayers for each subsequent violation of the City's Code would result in increased revenue of approximately $939,800 annually.

Furthermore, the Business Tax Division may not forward delinquent business tax accounts to the Investigations Division for over a year and the Investigations Division makes these accounts its lowest priority. As a result, collections are not maximized. Delinquent business tax accounts should be forwarded to the Accounting and Collections Divisions for follow-up within 60 days. More reasonable estimates of delinquent business taxes owed, plus imposing penalties, and expediting notices to delinquent taxpayers would eliminate these problems and encourage taxpayer compliance.

In order to obtain maximum benefit from the recommendations made in this Section, the Tax Collector should streamline and prioritize overall collections efforts.

Section IV.2: Consolidated Collections Process

Currently, three separate divisions of the Tax Collector's Office are responsible for delinquent revenue collection. If an accountholder owes more than one type of delinquent revenue, collections personnel pursue these various outstanding debts separately. The Tax Collector should consolidate the Investigations Division, the Bureau of Delinquent Revenue, and the Legal Division under a single manager.

Tax Collector personnel also use expensive labor intensive collections methods: letters are not mailed to delinquent accountholders automatically (although some BDR staff persons do mail letters at their discretion); only BDR seizes checking accounts and the Investigations Division makes in-person visits to collect delinquent UPP taxes. The Tax Collector should use less expensive non-labor intensive collections methods as a first step in collecting delinquent revenue. In addition, working with the Board of Supervisors, the Tax Collector should begin seizing checking accounts of delinquent business taxpayers and obtain Peace Officer authorization for issuing citations as an additional enforcement tool.

The Tax Collector has not established a multi-variable, automated prioritization system to ensure that accounts that would likely result in the highest return are pursued first. Functions in the legal sphere — i.e., seizures, small claims, bankruptcy, and major claims — are performed in separate locations, without legal oversight except in the case of major claims. The Tax Collector should establish a prioritization system for the collection of all delinquent revenue, ranked by collectability, amount and time limitations.
Costs for implementing these recommendations would be based on the Tax Collector's substantiated need for increased personnel. Implementation of the recommendations contained in this Section would result in estimated increased revenue of $150,000 to $1.5 million annually.

The Budget Analyst notes that the Board of Supervisors approved an Amnesty Program in September, 1994. Under this Program, delinquent taxpayers had a two month period (December 1, 1994 through January 31, 1995) during which they could apply for tax amnesty. The amnesty involved a waiver of all penalties, in exchange for payment of all delinquent taxes and interest due. As a result of the legislation approved by the Board of Supervisors, the Tax Collector has collected approximately $3.9 million from delinquent taxpayers who filed for amnesty. The program also helped the Business Tax Division to purge its database of an as yet undetermined number of inactive accounts (e.g., businesses that have closed or ceased to conduct business in San Francisco). At the same time, at least 215 previously unregistered businesses completed registration applications.

The current Tax Collector is committed to improving and reforming his operations. This commitment is demonstrated through his support of Total Quality Management (TQM) efforts as well as his active participation and assistance in the research and evaluation included in this report. We applaud his efforts in that regard and in numerous other areas where he has improved the

operations of the Tax Collector's Office. The Tax Collector's Office is anticipated to collect over $1 billion in FY 1994-95, including property taxes, business taxes, and other local fees and taxes. Nevertheless, the Budget Analyst has identified major findings in the Tax Collector's Office which require immediate attention in order to prevent the City and County of San Francisco from losing millions of dollars in annual revenues, as summarized above.

Respectfully submitted,

Harvey M. Rose
Budget Analyst

cc: President Shelley
Supervisor Alioto
Supervisor Ammiano
Supervisor Bierman
Supervisor Hallinan
Supervisor Kaufman
Supervisor Kennedy
Supervisor Leal
Supervisor Migden
Supervisor Teng
Clerk of the Board
Mayor Jordan
Mary Callanan, Treasurer
Richard Sullivan, Tax Collector
William Lee, Chief Administrative Officer
Edward Harrington, Controller
Teresa Serata
Robert Oakes
Ted Lakey

TABLE OF CONTENTS

LIST OF TABLES

LIST OF TABLES (continued)

LIST OF CHARTS

INTRODUCTION

The Budget Analyst's Office has conducted a *Management Audit of the San Francisco Tax Collector's Office.* The Board of Supervisors requested this study to assist the Tax Collector in his efforts to improve the efficiency and effectiveness of his Office. This report contains recommendations that will reduce the costs of the Tax Collector's operations, increase revenues from delinquent and newly identified taxpayers, improve taxpayer assistance, and improve internal controls.

Full implementation of the recommendations contained in this performance evaluation would decrease the Tax Collector's overall costs and increase revenues by a net amount of approximately $7.1 million to $16 million annually for the City. These projected revenues do not include an additional $14.3 million annually from unregistered businesses unpaid Payroll and Gross Receipts Taxes. Depending on future legal and policy decisions, the City could realize an additional $3.5 million to $6.9 million of one-time retroactive payments. Furthermore, because of the limited data available, many of the proposed recommendations could not be quantified, although implementation of such recommendations (such as an expedited Business Tax delinquent collections process) are likely to result in significant further savings, reduced costs, enhanced efficiencies and increased revenues for the City. Implementation of these recommendations may require an additional one-time net cost of $215,426.

Project Scope

The scope of this *Management Audit of the San Francisco Tax Collector's Office* is comprehensive. In summary, the scope of our study included a review of the following:

- √ The department's organization and staffing;
- √ Administrative functions, including accounting, data processing and automation;
- √ The department's cashiering and money-management activities;
- √ Taxpayer assistance coordination and provision;
- √ The licensing function within the Tax Collector's Office and a limited review of licensing functions within the user departments;
- √ Auditing of business taxpayers;
- √ Identification of businesses that must register with the Tax Collector and implementation of business registration activities;
- √ Legislative requirements and changes and their impacts on the operations of the Department;

- √ Regular (i.e., non-delinquent) billing and payment processes for all revenue types, including business and property taxes, business registration fees, licenses, and fees for City services (such as Hospital billings).
- √ Determination of delinquent revenue, including the business tax audit function and processes for estimating and notifying delinquent taxpayers of outstanding debts;
- √ Collection of delinquent revenue, with particular emphasis on resource maximization;
- √ Communication within the divisions of the Tax Collector's Office and City-wide; and
- √ The Tax Collector's past and current efforts to reorganize the department and make operational improvements, including the commencement of Total Quality Management.

METHODOLOGY

We conducted this management audit in accordance with the standards described in *Government Auditing Standards, General Standards, Field Work Standards for Performance Audits, and Reporting Standards for Performance Audits, 1994 Revision,* issued by the United States General Accounting Office, Comptroller General of the United States. As described by the Comptroller General, "These standards pertain to the auditor's professional qualifications, the quality of audit effort, and the characteristics of professional and meaningful audit reports."

We used the following general methodology to conduct this management audit:

- *Development of a Detailed Work Plan and Project Schedule*
  During the initial stage of the study, we conducted interviews with the Tax Collector, the Treasurer, and division managers in the Tax Collector's Office to obtain a broad overview of operations and matters of importance or concern to the Tax Collector. Also, we collected and reviewed previous studies and analyses of the Tax Collector's Office. These activities are called a pre-audit survey.

  Based on our pre-audit survey, we developed a detailed work plan and schedule for conducting the management audit, and met with the Tax Collector to review this work plan. The work plan included the specific areas for review, the approximate allocation of staff resources, and projected completion dates.

- *Review and Analysis of Department Operations*
  Using our detailed work plan as a guide, we began a systematic review and analysis of each targeted area of the Tax Collector's operations. This review included the following:

Interviews and Observations
We conducted interviews with management, supervisors, and line staff, and with appropriate other parties, such as representatives of the City Attorney's Office, the Controller's Office, the Assessor's Office, the Recorder's Office, user department representatives (including Police, Fire, Health, Animal Care and Control, Rent Board, and Public Works), and representatives of non-County agencies, such as the Internal Revenue Service, the State Board of Equalization, and the Franchise Tax Board. In addition, we observed Tax Collector activities, including riding along with Collections Investigators in the field and observing the taxpayer assistance desk.

Sampling
We conducted three different sampling activities. First, we visited five major commercial complexes, which included over 350 businesses, to determine the extent to which the Tax Collector has identified all businesses that must register. Second, we tracked four businesses previously delinquent in paying taxes to determine the delinquent tax collection process. Third, we reviewed 84 business registration forms to determine the extent to which the Tax Collector recorded changes of address correctly.

Survey
We conducted a written survey of six California jurisdictions to obtain comparative information on all aspects of the Tax Collector's activities, such as staffing levels, collections processes, identifying taxpayers, billing consolidation, use of contractors, amnesty programs, and automated financial reporting systems. Our analysis of this survey information is integrated into our report. Also, we surveyed four Bay Area jurisdictions to obtain comparative information on dog licensing programs, and nine Bay Area jurisdictions to obtain comparative information on dog licensing fees. In addition, we contacted various cities and counties in California to discuss alternative collection strategies.

Document Review
We conducted extensive reviews of printed information, such as:

- √ Budget documents;
- √ Policies and procedures manuals;
- √ Published information on government revenue and revenue collection functions, including textbooks, articles, published studies, and pamphlets;
- √ Local, State, and Federal legislation defining the role, powers and obligations of the Tax Collector and the City in collecting revenue;
- √ Reports indicating the Tax Collector's performance, including revenue and expenditures by division, by month, and by staff;
- √ Reports prepared by the Tax Collector's Total Quality Management (TQM) teams, and
- √ Various other documents, as appropriate.

- *Development of Recommendations and Report Writing*
  Based on our systematic review and detailed analysis, we developed specific findings and recommendations for improving the Tax Collector's operations (including improving efficiency, internal controls, and taxpayer assistance) and identifying policy decisions that must be addressed by the Tax Collector and the Board of Supervisors. We presented a draft of these findings and recommendations to the Treasurer and the Tax Collector. After reviewing comments and modifying our report where appropriate, we prepared and delivered our final report.

This project was initiated with an entrance conference with the Treasurer and Tax Collector and a separate meeting with the Tax Collector and his eight division managers. These initial meetings were held in November, 1994. We continued our field work through February, 1995, and submitted a draft report to the Treasurer and Tax Collector on March 23, 1995. The exit conference took place two weeks thereafter. We invited the Tax Collector to submit a written response to this report, which is attached as an appendix.

OVERVIEW OF TAX COLLECTOR OPERATIONS

The Tax Collector's Office is a division of the Treasurer's Department. The Treasurer is an elected official, and the Tax Collector is appointed by the Treasurer and serves at her pleasure. The Tax Collector, with the assistance of an Assistant Tax Collector, is responsible for the collection, receipt and deposit of all monies for taxes, licenses, and other fees due to the City and County, (except the sales and real property transfer taxes,) amounting to over $1 billion annually. Also, the Tax Collector collects delinquent accounts due to all City departments. These responsibilities of the Tax Collector are specified by the City's Charter.

The Tax Collector's Office:

- Identifies businesses that must register, bills such businesses, collects and deposits business registration fees, and issues Business Registration Certificates;

- Processes City business tax returns, collects and deposits business taxes, reviews and audits business tax returns, and pursues delinquent business tax collection;

- Administers business and individual license renewals for six user departments, including the Police Department, the Fire Department, the Department of Public Health, the Department of Animal Care and Control, the Rent Board, and the Department of Public Works. License administration includes billing, processing, license issuance, and delinquent revenue collection;

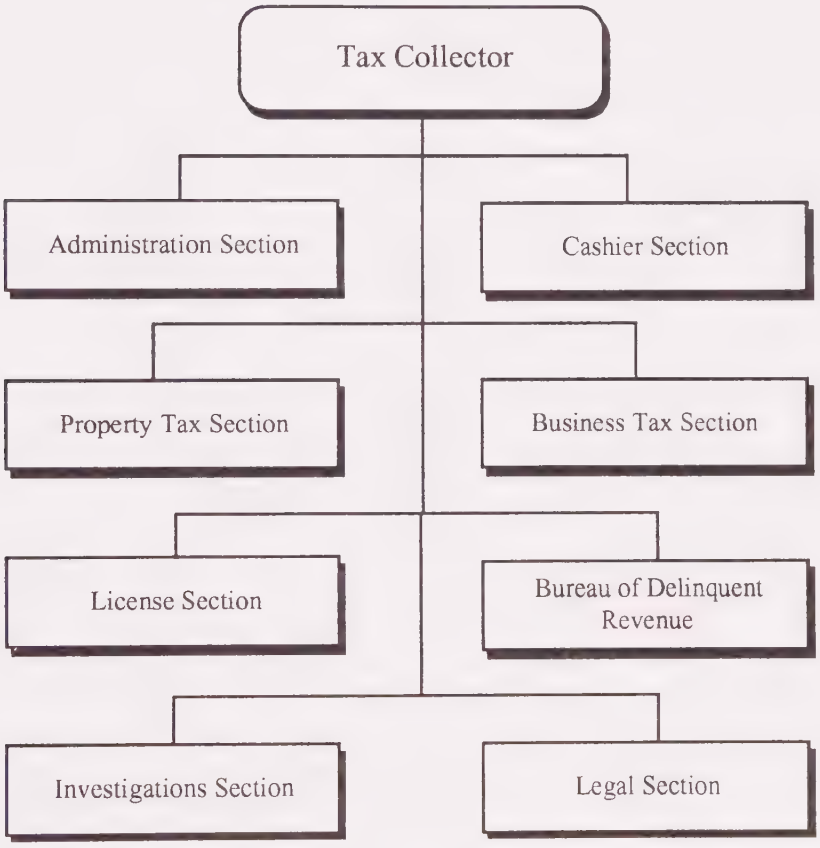
- Collects and deposits delinquent fees for service for all City departments, including in-house collection and collection contract management. The largest user department for this service is San Francisco General Hospital; and

- Administers property tax collection and special assessment district taxes that are attached to property.

To perform these functions, the Tax Collector's Office is organized into eight divisions under the Tax Collector and the Assistant Tax Collector: (1) Administration; (2) Business Tax; (3) License; (4) Cashier; (5) Delinquent Revenue; (6) Property Tax; (7) Investigations; and (8) Legal. Each division is overseen by a division manager. The following page includes an organization chart of the Tax Collector's Office.

Chart 1

Tax Collector's Office Current Organization



The Tax Collector is responsible for collecting all taxes, fees and licenses, except the sales tax (which is collected by the State), and the real estate transfer tax (which is remitted to the Recorder). The following table indicates the types of revenue collected by the Tax Collector, and the amount of revenue collected in that category, for FY 1993-94 and projected for FY 1994-95. This table does not include delinquent revenues collected by the Tax Collector for other City departments.

Table 1
Revenue Collected by the Tax Collector[1]
FY 1993-94, 1994-95

	Actual FY1993-94	Projected FY1994-95
PROPERTY TAXES		
General Fund	$331,240,000	$337,841,000
Other Agencies[2]	326,547,000	326,547,000
Total Property Taxes	657,787,000	664,388,000
BUSINESS TAXES		
Business Registration Tax	7,893,000	8,195,000
Gross Receipts Tax	23,856,000	22,555,000
Payroll Tax	132,595,000	134,467,000
Total Business Taxes	164,344,000	165,217,000
OTHER LOCAL FEES AND TAXES[3]		
License Fees, General Fund	5,080,000	5,155,000
License Fees, Other Funds	4,348,000	4,348,000
Hotel Room Tax, General Fund	28,054,000	29,980,000
Hotel Room Tax, Other Funds	56,108,000	59,960,000
Utility Users Tax	46,577,000	50,932,000
Parking Tax, General Fund	26,089,000	12,900,000
Parking Tax, Other Funds	6,522,000	19,350,000
Franchise Tax	7,149,000	7,129,000
Admission Tax	2,002,000	1,922,000
Vehicle Renter Tax	1,323,000	1,520,000
Total Other Local Taxes	183,252,000	193,196,000
TOTAL REVENUES COLLECTED BY THE TAX COLLECTOR	$1,005,383,000	$1,022,801,000

As indicated above, the Tax Collector received and processed payment for a total of approximately $1.005 billion during FY 1993-94, in property taxes, business taxes and other local fees and taxes. The Tax Collector's Office is anticipated to collect total revenue of approximately $1.023 billion in FY 1994-95. Although the Tax Collector does not have information about total current delinquent local taxes and fees, as of June, 1994, the Tax Collector reported to the Budget Analyst that $144 million in Business (Gross Receipts and Payroll) Taxes was outstanding. However, as noted in Section IV.1 of this report, this $144 million represents an intentionally inflated estimate, due to the Tax Collector's policy of estimating Business Taxes for businesses that do not file tax returns at 150 percent of the previous year's taxes.

---

[1]Sources: Schedule of Budgeted and Projected Revenues, Fiscal Year Ending June 30, 1995 as of December 31, 1994, "1994-95 Six Month Budget Status Report," Office of the Controller; and data on Property Tax Collections provided by the Controller.

[2]The Controller's Office could not provide projections for this revenue category for FY 1994-95, so we have assumed FY 1994-95 revenues equal to actual FY 1993-94 revenues.

[3]This listing of other local fees and taxes does not include the sales tax, and the real property transfer tax, which is paid to the Recorder. Neither tax is administered by the Tax Collector's Office, although the Tax Collector's Cashier processes the monthly sales tax remittance from the State.

In FY 1994-95, the Board of Supervisors authorized total budgeted expenditures for the Tax Collector's Office of approximately $10,236,800, as shown below:

Table 2

Tax Collector Expenditures by Division
FY 1993-94 and FY 1994-95

Division	FY 1993-94 Actual Expenditures Amount	Percent	FY 1994-95 Budgeted Expenditures Amount	Percent
Administration[4]	$835,389	9.1%	$887,035	8.7%
Business Tax	3,041,355	33.1	3,376,485	33.0
License	719,461	7.8	973,931	9.5
Cashier	340,361	3.7	348,957	3.4
Delinquent Revenue	1,596,811	17.4	1,672,179	16.3
Property Tax	1,142,837	12.4	1,333,208	13.0
Investigations	1,118,575	12.2	1,323,629	12.9
Legal	390,706	4.3	321,384	3.2
TOTAL	$9,185,495	100.0%	$10,236,808	100.0%

The Board of Supervisors authorized a total of 137 positions for the Tax Collector's Office in FY 1994-95. These positions are allocated as follows:

Table 3

Tax Collector Authorized Positions by Division
FY 1994-95

Division	Positions	Percent of Total
Administration	13	9.5%
Business Tax	46	33.6
License	8	5.8
Cashier	8	5.8
Delinquent Revenue	21	15.3
Real Estate	14	10.2
Investigations	22	16.1
Legal	5	3.7
TOTAL	137	100%

[4]Administration Division expenditures include Treasurer and Tax Collector's Office.

In FY 1994-95, the Board of Supervisors approved six new positions[5] to assume administrative and clerical duties currently being performed by auditors in the Business Tax Section, at a total cost of $363,331, including salary and fringe benefits. In addition, the Board of Supervisors approved the addition of three new Collection Officer positions for FY 1994-95, at a total cost of $152,646. The new staff additions were justified by the Tax Collector on the basis of projected new revenue generation. The Controller certified projected net new revenues for the Tax Collector's Office of approximately $300,000 in FY 1994-95. However, as of the writing of this report, the Tax Collector is still in the process of hiring these new positions; therefore, no new revenue has been generated as a result of these newly approved positions. Nevertheless, the Tax Collector's overall FY 1994-95 revenues should exceed budgeted levels because the Amnesty Program is expected to yield approximately $3.9 million during FY 1994-95.

SURVEY OF CALIFORNIA JURISDICTIONS

As part of this study, we conducted a survey of eight jurisdictions, including Denver, Colorado, a city and county, and the following six California jurisdictions: Los Angeles County, City of Los Angeles, San Jose, City of Sacramento, Orange County, and the City of San Diego. The purpose of this survey was to obtain comparative information to assist us in evaluating the San Francisco Tax Collector's Office and developing recommendations for operational improvements.

We selected the survey jurisdictions based on the following:

- *Population*
  All of the survey jurisdictions have populations over 100,000.

- *City / County Relationship*
  We surveyed two counties, four cities, and one city and county, because cities and counties have different obligations and powers in regard to revenue collection, and San Francisco is a city and county. In general, counties, which have tax collectors, collect property tax and special assessment district revenues. Cities, which generally have departments of revenue, collect user and license fees and, where relevant, business taxes. Denver, Colorado, like San Francisco, is a city and county.

- *Innovative Jurisdictions Identified by the Tax Collector*
  We included the City of San Diego in our survey because that jurisdiction had been identified by the Tax Collector as an innovative revenue collecting organization.

Information from our survey appears in the relevant sections of our report.

[5] 1822 Administrative Analyst; 1818 Senior Information Systems Specialist II; 1656 Head Accountant; 1654 Senior Accountant; 1632 Senior Account Clerk; 1630 Account Clerk

TAX COLLECTOR'S ACCOMPLISHMENTS

A management audit, by its nature, focuses on the weak areas of a department's operations, since the purpose of a management audit is to identify areas for improvement. In each of the remaining sections of this report, we provide a critical evaluation of services in order to clarify our perspective on operations and justify the need for change. We would be remiss, however, if we did not recognize the accomplishments of the Tax Collector's operations. The following paragraphs reflect some of these accomplishments.

Restructuring Effort

In June, 1993, the previous Tax Collector began a restructuring effort. This effort consisted of meetings with the then-Assistant Tax Collector and the Division Managers to identify areas in need of improvement and to implement reform. The outcome of these meetings was the establishment of a Single Point of Contact (SPOC) desk, where taxpayers can contact a single taxpayer assistance representative to receive answers to all tax collection-related questions.

The previous Tax Collector retired in June, 1994, and the new Tax Collector has expanded the restructuring effort to instigate Total Quality Management (TQM). TQM is a management reform method involving the active participation of line staff in improving departmental operations. Through TQM, the Tax Collector has issued two reports. The first, by *Task Force Bravo*, evaluates the provision of taxpayer assistance in the Tax Collector's Office, and recommends the establishment of a unit dedicated to this function. The second, by *Task Force Charlie*, discusses accounting functions in the Tax Collector's Office, and recommends that accounting functions be consolidated. Both reports provide useful analyses and recommendations for change. We refer to these TQM reports where appropriate in the following report.

The Tax Collector has demonstrated a strong commitment to improving and reforming his operations. This commitment is demonstrated through his support of TQM as well as his active participation and assistance in the research and evaluation included in this report.

Cashiering

The Cashier Division has made substantial improvements in depositing income as quickly as possible. Based on recommendations from the 1981 audit of the Tax Collector's Office performed by the Budget Analyst's Office, the Cashier Division has implemented automated payment processing. Implementation of this system has allowed the Cashier Division to process and deposit, on average, 80 percent of the days receipts by 4:00 PM. Within 24 hours, 90 percent of a days' receipts are processed and deposited. The remaining 10 percent that must be researched and reconciled are generally processed within five days of receipt.

Amnesty Program

The Business and Payroll Tax Amnesty Program was approved by the Board of Supervisors in September, 1994. Under the program, delinquent taxpayers had a two month period, (December 1, 1994 through January 31, 1995), during which they

could apply for tax amnesty. The amnesty involved a waiver of all penalties, in exchange for payment of all delinquent taxes and interest due.

As of the writing of this report, the Tax Collector had not yet entered the Amnesty Program application data into the computer program that was being prepared by the Controller's Information Services Division (ISD) to facilitate analysis of the program. However, the Tax Collector was able to inform us that approximately $3.9 million was collected from delinquent taxpayers who filed for amnesty. The program also helped the Business Tax Division to purge its database of an as yet undetermined number of inactive accounts (e.g., businesses that have closed or ceased to conduct business in San Francisco). At the same time, at least 215 previously unregistered businesses completed registration applications.

Business Identification

Over the last few years, legislation has been enacted to ensure that more businesses register with the Tax Collector. For example, since 1993, businesses must show proof that they have registered in order to record a fictitious business name statement with the County Recorder's Office. This is an excellent control, because businesses that do not operate under the owner's name must file a fictitious business name statement to open a bank account in the City. Other legislation has been passed to require businesses to show proof of registration prior to receiving City services. For example, the Board of Supervisors approved an ordinance in March, 1995 withholding residential parking permits from businesses pending proof of registration. In Section III.3 of this report, we recommend additional changes to increase identification of previously unregistered businesses.

Sales Tax Revenue Maximization

During the past year, the Tax Collector and the Controller jointly entered into a contingency fee contract with a consultant to identify misallocations of sales tax by the State Board of Equalization, in order to maximize sales tax returns to the City. Although the program has not yet generated new revenues, the Controller's Office advised us that the consultant estimates annual new City revenues of up to $500,000 from this program. Our contacts with other jurisdictions suggest that this is a valuable activity that can yield significant returns when fully operational.

Automated Systems

Over the past six years the Tax Collector's Office has made significant progress toward the automation of tax collection and recordkeeping functions. The Tax Collector has developed and implemented a Business Tax System that contains records of all business taxpayers and non-taxpaying registered businesses. Additionally, the Investigations Division automated historical information maintained on delinquent Unsecured Personal Property taxes and subsequent payments.

In addition to the two mainframe systems noted above, the Tax Collector's Office is in the process of converting a Wang Mini-Computer System to a Novell Local Area Network (LAN) environment. The new LAN operating environment will give the Tax Collector's staff the ability to use Personal Computer (PC) applications to complete routine assignments and conduct specially designed queries of data

contained in the mainframe systems. This change should: automate account and payment reconciliation processes; enhance communications through the use of CC-Mail and shared directories; and enable staff to generate ad hoc reports through the use of PARADOX.

The full benefits of these automation improvements are not being realized, because staff do not know how to make full use of the systems. Automation training needs and system modifications are outlined in Section I.2 of this report.

NEEDED OPERATIONAL IMPROVEMENTS: RECOMMENDATIONS AFFECTING ALL DIVISIONS

Throughout this report, there are some recurring themes related to the maximization of existing resources. The operational effectiveness of the Tax Collector's Office could be considerably enhanced by incorporating the following general categories of recommendations into the Tax Collector's management strategy:

- *Prioritization*
  Throughout the Tax Collector's Office we observed inadequate attention paid to prioritizing work. The Audit Unit of the Business Tax Division selects accounts for audit based on informal rules of thumb, rather than a uniform, sophisticated selection process that would prioritize accounts for audit based on clear criteria. (See Section III.1.) The three Divisions that collect delinquent revenues (the Investigations Division, the Bureau of Delinquent Revenue and the Legal Division) have no consistent process for prioritizing collections activities, to determine which accounts to pursue and how far to pursue them. (See Section IV.2.) Accounting and data entry activities would also benefit from conscious prioritization, so that management can establish and enforce productivity standards for key functions. (See Section I.1).

- *Cross-Training*
  The staff of the Tax Collector's Office would benefit from having a broader understanding of the functions of the Office, because (1) many functions are interrelated and interdependent, and staff needs to know how their work effects the work of others; and (2) the seasonal nature of tax collection leads to varying peaks and valleys in workload in the Tax Collector's Office, which could be managed more efficiently if staff were cross-trained.

- *Use of Automated Systems*
  As documented throughout this report, particularly in Section I.2, the Tax Collector has installed automated systems that have the potential to improve the speed and accuracy of many operations. However, the Administration Division should provide system overview training and extensive follow-up training to ensure that staff actually use the systems properly. Staff evaluations should include an appraisal of their use of automated systems, and managers should be evaluated on their success in achieving fluency on automated systems among the personnel they supervise.

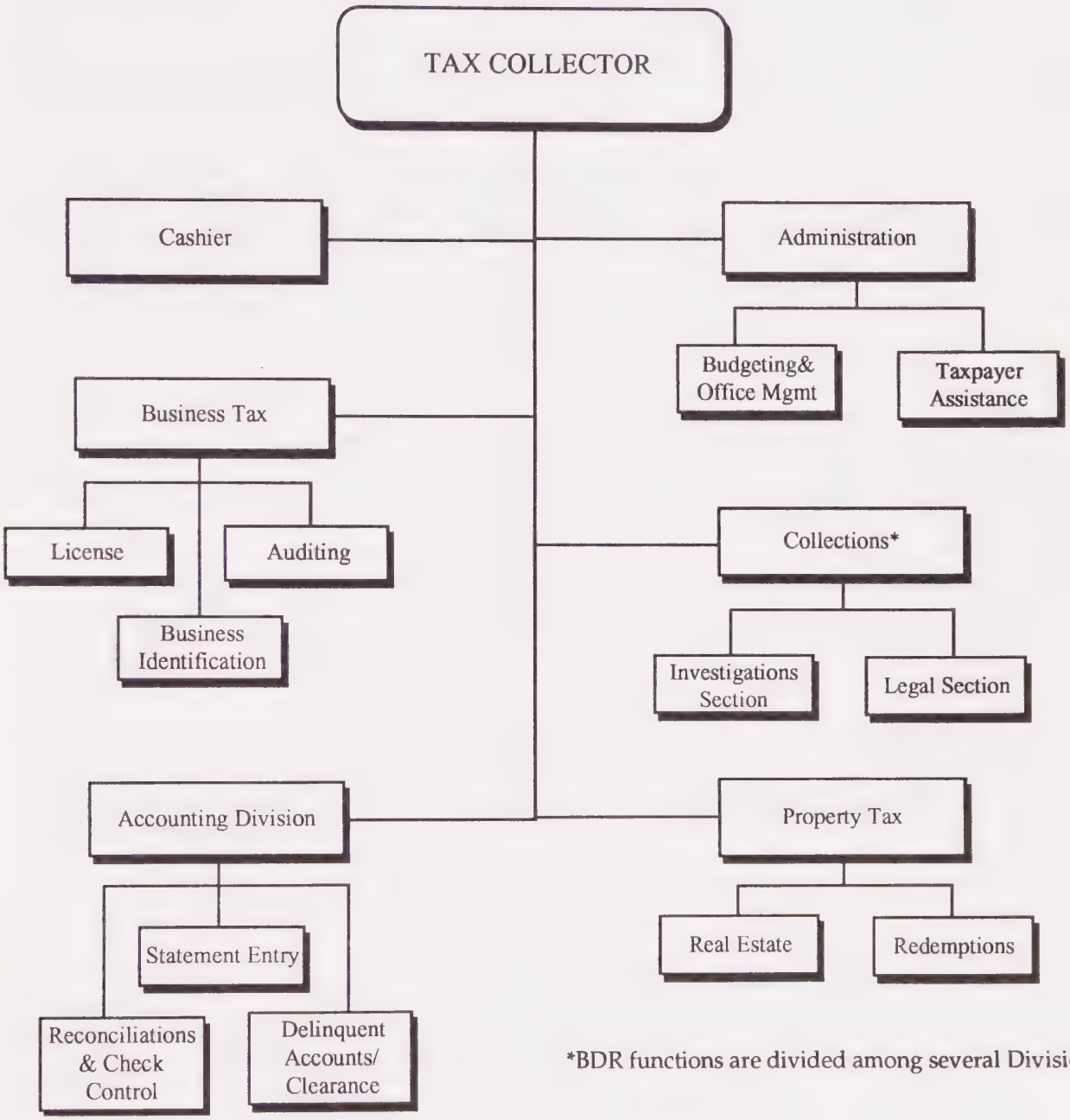
DEPARTMENT ORGANIZATION: AN OVERVIEW OF RECOMMENDED CHANGES

The following sections of our report include various recommendations that will result in restructuring several of the Tax Collector's divisions. Each of these recommendations was designed to enhance taxpayer assistance, improve internal controls, improve operational efficiency and/or to increase collection of tax revenues due the City.

The following paragraphs provide an overview of these changes. The purpose of this overview is to provide the reader with a high-level understanding of the overall organization of the Tax Collector's Office, pursuant to our recommendations. The specific costs, benefits, and parameters of these changes are provided in detail in our report; these paragraphs provide a high-level summary only. The following page includes an organization chart showing the new recommended structure of the Tax Collector's Office. This organization chart can be contrasted with the chart of the Tax Collector's present organization, as shown on page 5.

Chart 2

Tax Collector's Office Proposed Organization



*BDR functions are divided among several Divisions

The following summarizes our recommendations related to the Department's organization that follow this introduction:

- The total number of Divisions in the Tax Collector's Office would be reduced from eight to six, through the elimination and consolidation of three Divisions, and the addition of one new division, as follows:
  - √ The License Division's responsibilities would be dispersed and the License Division eliminated;
  - √ The Investigations Division, the Bureau of Delinquent Revenue, and the Legal Division would be combined into a single Collections Division; and
  - √ Certain personnel with accounting responsibility would be moved from their current locations to a centralized Accounting Division, resulting in improved checks and balances and greater efficiency. Data processing, in service of the long-term goal of linking all of the Tax Collector's automated systems. However, as noted in the Automation Section of this report, the consolidation of data processing may not occur until after the Department has improved its use of automated systems.

- A Taxpayer Assistance Unit would be created and placed under the Administration Division. Taxpayers would be able to approach knowledgeable taxpayer assistance representatives with access to complete, up-to-date information about their accounts.

- A Business Registration Program, with explicit responsibility for identifying businesses, maintaining Business Registration Certificate records and implementing billing would be created and placed under the Business Tax Division, to be staffed by a new Limited Tenure 1832 Management Analyst.

- Responsibility for collecting license fees would be divided among the Property Tax Division, which would have responsibility for property-related licenses (i.e., the Rent Stabilization and Arbitration fee and apartment house license fees), and the Business Tax Division which would have responsibility for business-related licenses and individual licenses (specified in our report). The Department of Animal Care and Control would assume responsibility for dog license administration.

- A new delinquent revenue collection process would be created, beginning with mailing of at least two accurate, complete payment demands by the new Accounting Division. The new Collections Division would seize financial assets and place liens before beginning more labor-intensive forms of collection. Other types of collections would be prioritized according to the recommendations contained in this report, and Collections Division personnel would be assigned specialties according to the priorities established through these measures.

DEPARTMENT STAFFING LEVELS: GUIDELINES FOR FUTURE EVALUATIONS

Until the Tax Collector has implemented these broad changes in departmental operations, it will be difficult to analyze the department's staffing needs. For example, consolidated billings might result in decreased demand for taxpayer assistance, because taxpayers will receive a single, clear bill from the Tax Collector's Office. Similarly, improvements in automation might result in a decreased need for clerical support. The following paragraphs describe our observations about current staffing, and our recommended methods for evaluating the Department's staffing needs in the future, after implementation of our re-organization recommendations.

Given the Department's current organization and procedures, we identified certain staffing deficiencies. For example:

- Business Tax Division auditors often provide taxpayer assistance and perform accounting functions, rather than perform audits;

- Additional collections personnel might result in additional net revenue;

- Certain functions that would generate revenue are not performed in a timely manner, or are not performed at all. For example, Business Tax Statements are not entered into the computer system for at least four months, creating a delay in processing delinquencies. Less than ten percent of delinquent business taxes are pursued by the Investigations Division. These deficiencies result from a number of factors, including inefficient use of existing resources, insufficient automation or incomplete use of existing automated resources. Insufficient staffing may also contribute; and

- Staffing allocation may not be optimal. For example, each Division has a separate budget to support temporary personnel; if workload peaks and valleys were timed appropriately, the Tax Collector might be able to create a permanent pool of generalists who could serve the different Divisions on an as-needed basis.

Because staffing needs will change significantly in response to organizational and operational changes, and also because certain policy decisions (as identified in this report) must be made to determine desired levels of service, a staffing analysis was beyond the scope of this audit. However, we believe that the Tax Collector should conduct an analysis of the Department's staffing needs after the Tax Collector has implemented organizational reform. This analysis should take into account the following:

- *Policy Decisions*
  The Mayor, the Board of Supervisors and the Tax Collector must make certain policy decisions in regard to desired levels of service before a staffing analysis can be completed. Specifically, revenue maximization efforts may

have a cost in taxpayer relations: relentless, aggressive pursuit for little return can result in taxpayer dissatisfaction. For example, a taxpayer might owe outstanding fees or taxes of $100. The Tax Collector could expend $200 to collect that $100 in delinquent revenues and pass that cost along to the delinquent taxpayer, at a total cost to the taxpayer of $300. While the City would realize an additional net $100 as a result of this pursuit, taxpayers might view this cost:benefit ratio — $2 spent for every $1 collected, or a 50 percent cost:benefit — as inappropriate. The Mayor, the Board of Supervisors and the Tax Collector need to weigh the benefit of the additional revenue against the cost in taxpayer relations when deciding the desired level of pursuit.

In addition, the Tax Collector's staffing requirements are affected when legislation pertaining to taxes is approved. As noted in Section III.1 of this report, Tax Collector resource requirements should be one consideration in approving tax-related legislation.

- *Efficiency*

  Efficiency improvements will decrease the Tax Collector's staffing requirements to provide the same level of services:

  √ *Automation*
  Maximizing the use of existing systems through training, providing automated video and telephone information, and obtaining scanning equipment are means through which increased or improved automation can reduce staffing requirements;

  √ *Seasonal Fluctuations and Pooling Resources*
  Due dates for taxes and fees, which are accompanied by workload increases, come at different times of the year. Due dates should be coordinated, and resources pooled, to improve the Department's resource utilization;

  √ *Personnel Management*
  The Tax Collector can enhance the productivity of existing personnel by providing appropriate supervision and evaluations, and, to the extent possible, creating incentives for good performance and sanctions against poor performance. Supervision and evaluation standards for auditors are discussed in Sections III.2 and III.2; general accounting performance goals are discussed in Section I.1.

  √ *General Operational Efficiencies*
  Many of the recommendations contained in this report will result in improved operational efficiencies, such as the consolidation of tax bills, the consolidation of accounting functions, and improved inter-divisional communications.

- *Circumstances Outside of Local Control*

  Certain circumstances outside of local control will impact the Tax Collector's staffing needs, as follows:

- √ *State and Federal Legislation*
  Changes in State and Federal legislation, mostly pertaining to property taxes and Medicare/MediCal for hospital bills, can impact the Tax Collector's resource requirements; and

- √ *Economic Health*
  The economic well-being of the State of California and of the City will impact the Tax Collector's needs. For example, reductions in the value of property result in decreased revenue but increased workload, since downward reassessments, and therefore property tax refunds, must be processed by the Tax Collector.

OBSERVATIONS AND COMMENTS

The success of the Tax Collector's Office is dependent in part on the productivity of other departments, particularly the Assessor's Office in regard to secured and unsecured property taxes, and the Controller's Information Services Division (ISD) in regard to the Tax Collector's automated systems. An evaluation of other departments whose activities might impact the Tax Collector's Office was beyond the scope of this report. However, it is worth noting that during the course of this audit, several questions were raised about the efficiency of the Assessor's Office. For example, certain property tax bills have failed to reach or have been delayed in reaching a property owner because the owner's billing address had changed, and the Assessor is not up-to-date in entering address changes. (According to the California Revenue and Taxation Code, only the Assessor is authorized to modify the Assessor's rolls, including inputting address changes, and the Tax Collector must use the address listed in the Assessor's rolls to implement billings.) As a result, tax payments have fallen into arrears, and the Tax Collector must collect on such delinquencies. This results in lost revenue, because collecting delinquencies is more labor intensive than regular on-time collections, and because any delays in payment costs money for the period during which delinquent collections takes place. In preparing this report, we did not include findings that resulted from deficiencies in other City departments that are outside of the control of the Tax Collector's Office.

ACKNOWLEDGMENTS

We would like to thank the Tax Collector, Mr. Richard Sullivan, and his staff, particularly the Division Managers, including Ms. Gail Friedlander, Mr. Patrick Sha, Ms. Anita Jin, Ms. Sonia Martinez, Mr. William Quong, Mr. Francis Nguyen, Mr. Robert Fletcher and Mr. Andy Bacigalupi, for their cooperation and assistance during the course of this management audit. We found the Tax Collector's Office to be consistently available and willing to share information throughout the preparation of this report.

SECTION I.1 : ACCOUNTING AND STATEMENTS

Accounting and data entry functions are currently distributed throughout the divisions of the Tax Collector's Office. Efficiency improvements that will increase revenue collections can best be implemented by establishing a consolidated Accounting Division, as recommended by the Tax Collector's Total Quality Management (TQM) Task Force Charlie.

Collections efforts are hampered by the nearly four month process of entering Business Tax Statements to the Business Tax System (BTS), which should be shortened by the planned introduction of scanners for statement entry. A centralized Accounting Division would provide an environment in which performance goals for statement entry could be monitored and enforced.

The fragmented check control process takes time away from revenue producing activities, costing the City an estimated $276,641 annually in foregone collections. Business Tax, License, Fees and Unsecured Personal Property Tax (UPP) check control should be centralized.

Tracking delinquent accounts can be improved in several ways. Use of BTS should be maximized to eliminate manual calculation of penalties and interest by multiple Divisions. The Accounting Division should cross-check delinquent UPP and Business Tax Accounts, so taxpayers can be notified of both delinquencies simultaneously, and Collections Officers can pursue full payment.

The Assessor's Office is responsible for substantial delays in posting reassessments in property values to the Tax Rolls. The Tax Collector should closely monitor and support the progress of automation efforts in the Assessor's Office.

The maintenance of accurate account data is essential to the ability of all divisions of the Tax Collector's Office to perform their functions. As part of this management audit, we examined the distribution of accounting and statement entry responsibilities throughout the Tax Collector's Office, and considered whether these activities could be administered more effectively.

Our analysis was formulated on the basis of interviews with division chiefs, key accounting personnel and staff of the Controller's Information Services Division (ISD), a review of organization charts to identify accounting and data entry personnel, and review of the Tax Collector's own internal Total Quality Management (TQM) analysis of accounting.[1]

We found that, as with taxpayer assistance, the Tax Collector has launched a planning effort to improve accounting procedures. The Tax Collector's report of Tax Force Charlie provides an overview of the goals of centralized accounting, although many aspects of the plan need more detailed examination. Specifically, we found that Business Taxes statement entry takes too long, but will likely be improved by the recent purchase of two scanners. (A scanner is a computer accessory that can automatically read and enter statements.) A centralized Accounting Division should take responsibility for achieving entry of all accounts within 30 days of the due date, and immediately thereafter mail the first letter to delinquent Business Taxpayers.

We also found that fragmented check control processing is being handled by revenue producing personnel (auditors and investigators), thereby costing approximately $276,641 in uncollected revenues. Tracking of delinquent accounts is hampered because certain Divisions make manual penalty and interest calculations, even though the BTS system is capable of making these calculations automatically. Furthermore, there is no current accounting activity to cross-check delinquent Unsecured Personal Property (UPP) and Business Tax accounts for billing and collections purposes, although the Clearance Unit of the Investigations Division does cross-check accounts prior to issuing Business Registration certificates.

This section of our report does the following:

- Describes the current organization of the Tax Collector's Office in regard to accounting and statement account entry;

- Identifies inefficiencies and opportunities for improvements in:
  - Business Taxes statement entry
  - Check Control
  - Tracking of Delinquent Business Taxes, Licenses and Fees
  - Tracking of Delinquent Unsecured Personal Property (UPP) Taxes
  - Clearance of Business Registrations

[1]"Final Report and Recommendations of Task Force Charlie," January 20, 1995.

Accounts Payable/Bank Account Reconciliation/Budget Assessor's Posting of Reassessment to Property Tax Rolls; and

- Establishes a recommended reorganization of accounting activities to improve collections and taxpayer assistance, and proposes automation improvements to increase efficiency.

CURRENT DISTRIBUTION OF ACCOUNTING ACTIVITIES

The Property Tax and Business Tax Divisions have primary responsibility for billing and accounts receivable in the Tax Collector's Office. The Cashiering Division plays a crucial related role in accepting payments from taxpayers and recording them in the City's main accounting system. However, each of the three Divisions that handle delinquent revenue collections -- Investigations, Bureau of Delinquent Revenue and Legal -- maintains separate records, as does the License Division. Finally, personnel in the Administration Division handle expenditure accounting (accounts payable). Descriptions of the functions performed in each Division of the Tax Collector's Office are provided below.

Cashier Division

The Cashier Division receives all payments to the Tax Collector, whether accepted over the counter in cash or by check, or received through the mail. Cashiers scan payment stubs into the City's Financial Accounting Management Information System (FAMIS), microfilm the checks, and submit the original checks for deposit. While cashiering is not an accounting function per se, a large portion of the accounting work of the Tax Collector's Office originates with the Cashier Division. Payment data input by Cashiers must be reconciled by other Divisions in the Tax Collector's Office with their own accounts payable databases, and problem checks -- that is payments that cannot be accepted by the automated accounting system because it is unclear how to credit the payment to a specific account -- are submitted by the Cashier to the Division that the Cashier believes will most likely have the information to resolve the problem.

Property Tax Division

The Property Tax Division is staffed almost entirely by accounting personnel, and all of this Division's functions are accounting functions, albeit with a heavy component of related taxpayer assistance. The Real Estate Director coordinates all billing for the Secured and Unsecured Property Taxes, based on data provided by the Assessor's and Controller's Offices.

A major accounting function of the Property Tax Division is processing the large number of Property Tax refunds that must be made, based on decisions of the Assessment Appeals Board. The refund workload has expanded in recent years, as real estate values have declined in the Bay Area. Currently, five 1630 Account

Clerks, supervised by a 1650 Accountant, handle the processing of Property Tax refunds and respond to the many taxpayer inquiries related to these refunds.

The Accounting Unit of the Property Tax Division sends out notices of intent to file liens for late current year Secured and Unsecured Property Tax bills. The 1630 Account Clerk and 1650 Accountant in this unit also perform reconciliation of daily and monthly postings by the Cashier to FAMIS with the Tax Collector's Secured and Unsecured Property Tax account databases.

Maintenance of account data related to delinquent Secured Property Taxes is performed by the Redemption Unit of the Property Tax Division. The Redemption database is used to record liens automatically on delinquent properties. Penalties and interest charges are calculated by the system, but a 1630 Account Clerk and a 1650 Accountant must separately enter payments of delinquent Secured Property Taxes to the Redemption database and manually release liens when full payment is made. The Redemption Unit also receives many inquiries from the public, particularly from banks and title companies that need to verify the status of liens on specific properties.

Finally, a 4306 Collections Officer in the Property Tax Division handles the research and disposition of checks received for payment of Property Taxes that cannot be accepted by the Cashier's remittance machine ("check control"). Most of these cases involve taxpayers who pay an amount based on a reassessment that has not yet been entered to the Property Tax Rolls by the Assessor. In addition, this Collections Officer bills taxpayers for bad checks received for payment of Property Taxes.

Business Tax Division

The Business Tax Division has primary responsibility for statement entry and account maintenance related to Business Registration and Business Payroll and Gross Receipts Taxes, Hotel Taxes, Parking Taxes, Utility Taxes and other business-related taxes, at least up to the point where these accounts are referred to Investigations for collection of delinquent revenue. Whereas basic property data is assembled and input by the Assessor's and Recorder's Offices, all information about firms doing business in San Francisco must be entered by the Business Tax Division to the Business Tax System (BTS).

The Business Tax Division coordinates the mailing of bills for the annual Business Registration Fee, the annual Business Payroll and Gross Receipts Statement, quarterly statements for large accounts and hotel/parking tax accounts, as well as annual Statements of Account and/or Business Tax Notice of Determination letters to delinquent business accounts.

Three 1424 Clerk Typists and a 1404 Clerk perform most of the statement processing functions for the Business Tax Division. This includes manual entry of the detailed information completed by businesses on their annual Payroll and Gross Receipts Tax Statement, and entering new account data for firms filing a

Business and Payroll Tax Application for the first time. Accounts also need to be manually updated for changes in address, ownership, etc.

The accounting functions performed by the Business Tax Division have been handled primarily by a team of five Auditors, a Senior Auditor and a Principal Auditor, with assistance from four 1630 Account Clerks and two 1632 Sr. Account Clerks. These functions include reconciliation of the Cashier's daily and monthly postings to FAMIS with BTS financial control reports, resolving problem statements for the statement processing staff, issuing refunds, approving requests for filing extensions, completing background paperwork on bad checks for referral to the Investigations Division, researching and answering correspondence from taxpayers, and processing check control. In the case of Business Taxes and Business Registration, the most common check control issues involve checks for which the Cashier is unsure of which account to credit, because the Federal Identification Number does not match the identification number that is in FAMIS, the ownership has changed, the check is sent without an accompanying statement, etc.

In addition to performing these standard accounting and statement processing functions, the Business Tax Division's auditing and accounting staff currently maintain separate records of audit deficiency accounts receivables, including manually adjusting for the accrued penalties and interest, and allocating payments that involve more than one tax year. Because of security-related computer access restrictions (described in Section I.2 on Automation), Auditors also are required to close accounts, and make other routine adjustments to account information that cannot now be performed by the statement processing unit.

Six new positions are authorized for the Business Tax Division in the FY 1994-95 budget, three of which were slated to join a newly organized Accounting and Statements Unit of the Business Tax Division. They are: a 1630 Account Clerk, a 1654 Principal Accountant, and a 1656 Head Accountant. The Tax Collector stated in his budget request that these new positions would relieve the clerical and accounting functions now performed by Auditors. However, only the 1630 Account Clerk had been hired as of the writing of this report. At full authorized staffing, the Business Tax Division Accounting and Statements Unit would have eight accounting personnel and four clerical personnel.

Investigations, Delinquent Revenue and Legal Divisions

The three Divisions of the Tax Collector's Office that are dedicated to collection of delinquent revenue -- the Investigations, Delinquent Revenue and Legal Divisions -- have minimal dedicated accounting staff. However, these Divisions do perform accounting functions. The Cashier refers problem checks for check control to these Divisions if the check appears to be payment on a delinquent account. As with the Business Tax Division, where Auditors currently perform check control,

in the three collections Divisions, Investigators, Collections Officers or Legal Assistants perform most of the research required for check control.

Besides assisting with check control, these Divisions maintain their own records of accounts referred to them, collections activity status, installment payment agreements, interest and penalty calculations, etc. Each Division assigns separate identification numbers to accounts based on their internal record-keeping system.

The Clearance Unit of the Investigations Division must be distinguished from the rest of the collections functions, as this unit performs a relatively complex accounting function. The Clearance Unit is responsible for checking the various account databases in the Tax Collector's Office to determine whether businesses applying for registration with the City have any outstanding balances due on City taxes or fees. Registration applicants with balances due are notified; those who are current in payments to the City are issued Business Registration Certificates. This task is currently performed by three 4306 Collections Officers, under the supervision of a 4334 Investigator.

License Division

The License Division's functions are largely accounting functions, in that the Division is responsible for implementing regular billing, processing payments (i.e., opening mail, entering data, and forwarding checks for deposit), and maintaining accounts information. In Section II.1 of this report, we recommend that the License Division be eliminated, and that license billings be combined with the Property Tax bill or the Business Registration bill. Therefore, in this section, we do not discuss the License Division's activities separately from the Property Tax and Business Tax Divisions.

Administration Division

The Administration Division handles budgeting and accounts Payable for the Tax Collector's Office. A 1220 Payroll Clerk and 1222 Sr. Payroll Clerk process payroll, and a recently hired 1654 Principal Accountant position processes all encumbrances, accounts payable, and petty cash involved with purchases made for the Tax Collector's Office. A 1408 Principal Clerk assists in processing accounts payable. (Until the recent authorization of the 1654 Principal Accountant position, Auditors had been assigned to reconcile expenditures to FAMIS.)

INEFFICIENCIES AND RECOMMENDED REMEDIES

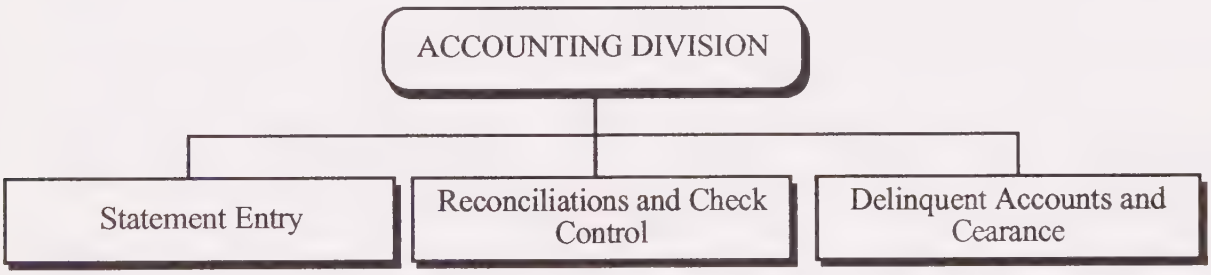
We identified inefficiencies in the Tax Collector's accounting and data entry practices that hinder collection efforts and complicate responses to taxpayer inquiries. These inefficiencies, and opportunities for improvement, are detailed below.

In addition to proposing the specific measures outlined below that can be taken to improve accounting practices, we endorse the recommendation of the Tax Collector's TQM Task Force Charlie to:

> ...develop a centralized, organized internal control unit to process taxpayers' accounts, to provide timely financial information to management, and to perform other accounting functions in an accurate, efficient manner within the Treasurer/Tax Collector Department.[2]

Many of the accounting and data entry problems detailed below are in part caused by the placement of critical accounting/data entry functions within specialized divisions of the Tax Collector's Office, so that the accounting/data entry functions are secondary to the real mission of each Division. As stated at the start of this section of the report, the quality of the Tax Collector's accounting systems is a key factor in the Tax Collector's ability to assist taxpayers and to maximize the collection of revenues for the City. A centralized accounting division (at least for Business Taxes, Licenses, and Unsecured Personal Property) would provide clear lines of responsibility for accounting tasks so that standards of account maintenance performance can be set, and actual performance can be compared with the standards.

A consolidated Accounting Division would include a Statement Entry Unit, a Reconciliations/Check Control Unit and a Delinquent Accounts/Clearance Unit, as diagrammed below:



Business Taxes Statement Entry

All registered businesses in San Francisco are required to submit an annual Business Tax Statement, even if they do not owe taxes. The statement includes information about the firm's identification number, location, mailing address, owner's name, type of business, tax rates, etc., as well as the financial information that is used by the business to calculate taxes due, such as the calculation for the Business Gross Receipts and Payroll to determine which is

[2]"Final Report and Recommendations of Task Force Charlie, "January 20, 1995, p. 2.

greater for estimating taxes due the City. The Tax Collector receives approximately 60,000 statements by the filing date of February 28 of each year.

The statements are entered manually to the BTS database in their entirety. This process generally takes the Business Tax Division approximately three months, in part because it is so labor intensive, and in part because the staff who do data entry and the accounting or auditing staff who assist them with complex or unclear tax statements may be called away to staff taxpayer assistance, do check control, or perform other immediate tasks. As a result, delinquent taxpayers -- those who have failed to file a statement -- cannot be informed of their delinquency status until mid- to late June, when the Business Tax Division estimates their taxes and sends them a "Letter of Determination."[3]

The four month time lapse between the date that an account becomes delinquent and the date that the taxpayer receives the first notice of the delinquency should not be tolerated by the Tax Collector, because accounts become less and less collectible as time goes on. Prompt notification would communicate a sense of urgency to the taxpayer, and at the same time give the taxpayer the opportunity to avoid costly interest payments.

We also observed a high error rate in the current data entry process. We sampled 84 address changes that had been submitted by businesses and entered to the BTS by data entry staff. We found that 13 of the 84 addresses had in fact not been updated in BTS. This represents a 15 percent data entry error rate. In practical terms, if the BTS system does not have the current business address, statements and delinquency notices may fail to reach the business owner, resulting in a potential loss of revenue to the City, aggravated taxpayers or a combination of both.

The Tax Collector was in the process of addressing these two statement entry problems at the time this report was written, through the purchase of two scanners. (As stated earlier, a scanner is a computer accessory that can automatically read and enter statements.) According to staff of the Controller's ISD, the Business Tax Division will be able to scan, rather than manually enter, approximately 80 percent of the Business Tax Statements that are received each year. The remainder -- those that have multiple business addresses or other complicating factors -- will at least initially still have to be entered manually to the BTS. The use of scanners should speed up the statement entry process significantly, and also reduce errors.

The ISD estimates that a data entry clerk will be able to scan 100 statements per hour. If the two scanners are used full time by clerical personnel, they should be able to complete scanning of the 80 percent of statements that can be scanned (approximately 48,000 statements if all registered businesses submitted statements) within 30 working days of the February 28 filing date. In order to process the 12,000 complex statements (a maximum number based on all registered businesses filing statements) within the same 30-day period, the

[3] See discussion of how determinations are calculated in Section IV.1.

Business Tax Division would have to devote enough clerical staff to the task so that an average of 50 statements could be processed each hour. The statements take five minutes, on average, to input manually, such that we estimate that up to four clerical staff would have to be allocated full time to the task.[4]

Once the scanners are purchased and staff is trained, the Tax Collector should establish a goal of processing all Business Tax Statements within 30 working days of the filing deadline, or approximately by mid-April. Achievement of this goal would greatly benefit the effort to collect delinquent Business Tax Accounts. The Accounting Division should implement a practice of mailing simple delinquency notices (i.e., without waiting for determination of the estimated taxes) to taxpayers who fail to file at the earliest possible date. Establishment of a consolidated Accounting Division should provide an environment in which these performance targets would be pursued more aggressively than under the current situation, in which statement entry personnel are not monitored closely, and are frequently called away from their task to assist with other activities of the Business Tax Division.

Check Control

The TQM Task Force provided a clear description of the inefficiencies associated with distributing responsibility for identifying the accountholders for payments that come without identifiers (i.e., check control). The Task Force Charlie report noted the following problems with the current check control procedures:

- Divisions within the Tax Collector's Office sometimes take too long to process a single check control. The report cited the Investigations Division, where each check control goes to the Chief Investigator for review, then to the Senior Investigator to log, then to the Investigator handling the account, then back to the Senior Investigator and to the Chief Investigator before being sent to the Cashier. The Investigations Division also has a separate Accountant position, which is not used for this check control accounting.

- A single check control may go to more than one Division, if two Divisions were involved in the collection of an account. For example, the report noted that checks related to a medical obligation would go to both BDR and the Legal Division; similarly, checks related to a delinquent Business Tax account might go to the Legal and/or Investigations Division as well as the Business Tax Division for check control, duplicating the required staffing efforts to resolve this accounting problem.

- In processing a payment, the Division that researches the problem check sometimes has to rely on another division to produce the stub that is

[4]Ideally, all statements would be entered by March 31 of each year, rather than April 15. If ISD estimates of scanning times are correct, this would necessitate use of temporary data entry clerks after normal business hours, when the scanners would be available. The Tax Collector should consider this option after scanners have been successfully incorporated into data entry operations.

needed by the Cashier to complete processing of the payment, again requiring an unnecessary duplication of effort.

We also found that the Business Tax Division uses a .4 FTE Auditor to process check control and the Investigations Division uses a .33 FTE Investigator. Such personnel are involved with direct revenue producing activities, such that diverting their efforts to check control reduces revenues. We estimate that the Tax Collector could recover approximately an additional $276,641 in annual revenues if check control were handled by accounting staff rather than audit and collections staff.[5]

Although the TQM task force recommended the centralization of all check control, we propose that the TQM implementation group start by centralizing Business Tax, Business Registration, and Licenses. Eventually, Unsecured Personal Property Tax (UPP) check control should also be centralized. However, it may be practical to leave Secured Personal Property Tax check control with the Property Tax Division, because the resolution of these check control problems frequently requires interaction with the Assessor's Office. The Property Tax Division is in the best position to accomplish this task. (Some interaction with the Assessor's Office will be required for UPP check control as well, but reassessments are less frequent for UPP than for secured property.)

Tracking of Delinquent Accounts

Business Taxes, Licenses and Fees

As described earlier, each of the Tax Collector's Divisions involved with collections currently maintains separate records on the accounts they are handling, even to the extent of assigning different account identification numbers to the same delinquent account. Furthermore, there is no one place in the automated systems where penalties and interest on delinquent accounts are calculated and updated. As stated in the TQM report, "...Many times, the figure (balance due) can be different depending on the particular division's calculations."

The lack of a centralized accounts receivable function to track delinquent accounts complicates the process of assisting taxpayers in obtaining up-to-date information on the status of their accounts (see Section I.3, Taxpayer Assistance). The absence of a unified, reliable automated procedure for tracking interest and penalties (as well as penalty waivers), installment payment arrangements, liens and seizure activities complicates the check control process.

---

[5] This revenues estimate includes the average annual revenues currently generated by .4 FTE Auditor ($141,353) and .33 FTE Investigator ($135,288), based on estimates of time spent on check control provided by their respective Division Chiefs. The $141,353 included here for auditor's time has also been incorporated into the calculation of revenues that could be generated by returning an entire audit team to audit work, from accounting and administrative duties. Please see Section III.1, Business Tax Auditing.

According to ISD staff, the Tax Collector's Office has discussed with them the need to revise the BTS to permit better tracking of delinquent accounts, but has not asked ISD to make this revision a priority. While we recognize the many competing needs for ISD's assistance, we recommend that the Tax Collector make this a high priority request to ISD, because the full benefits of centralized accounting -- for taxpayer assistance, check control and collections -- can only be achieved when tracking of delinquent accounts can be accomplished through one accounts receivable function. Once the BTS program is modified to handle delinquent accounts tracking, data on Business Taxes, Business Registration, Licensing and fees should be transferred from the separate tracking systems maintained by each Division to the BTS screens maintained by the proposed Accounting Division.

Secured and Unsecured Property Tax Delinquencies

The foregoing discussion of a centralized delinquent account tracking function did not pertain to delinquent Property Tax accounts. As with the check control process, the tracking of delinquent Secured Property Tax accounts should, at least initially, remain with the Property Tax Division. Unlike other delinquent taxes and fees, the Secured Property Tax has a "built-in" collections system, under which liens are automatically recorded against the subject property, which can be sold by the county to recover the taxes due after five years. Thus, the tracking of delinquent Secured Property Tax accounts is a relatively straightforward procedure that appears to be handled adequately by the Property Tax Division.

Although the Tax Collector has similar lien/sale powers for delinquent Unsecured Personal Property Tax accounts, in practice the Tax Collector could not take on the complex task of warehousing and selling the myriad types of taxable unsecured personal property. Currently, (as described in Section IV.2, Consolidated Collections,) delinquent Unsecured Personal Property Tax accounts are referred to the Investigations Division for standard collection efforts. It is therefore important for the Tax Collector to include tracking of delinquent Unsecured Personal Property Tax accounts as part of the responsibilities of the centralized Accounting Division that we have recommended, with other delinquent business taxes and fees.

A separate Unsecured Personal Property (UPP) database is currently maintained by the Property Tax Division. Although most UPP taxpayers are businesses, and the Clearance Unit (which checks for taxes due prior to issuing Business Registration Certificates) reports that most delinquent UPP taxpayers also owe Business Taxes, there is no direct way to correlate UPP accounts with BTS accounts. Taxpayers are billed separately for UPP and Business Taxes, and receive separate delinquency notices for each type of tax if they fail to pay on time. As described (in Section IV.2, Collections), Investigators devote most of their time to collecting delinquent UPP taxes -- without any knowledge of whether they should also be demanding payment of delinquent business taxes. This is clearly a costly inefficiency that should be addressed by accounting managers.

ISD personnel advised the Budget Analyst that in order to create a fairly quick and easy way to cross check UPP and BTS accounts, the two databases would need to share an identifying field. They suggested that the owner's Social Security number, or the Federal Employers Identification Number (FEIN) would be the most practical. However, the Assessor maintains that he cannot release this information to the Tax Collector relative to UPP accounts, because it must, by State law, remain confidential. Because of the significant opportunity to increase collection of taxes owed the City, we recommend that the Tax Collector and the Assessor work with the City's elected State representatives to effect any needed changes to the State Revenue and Taxation Code, to enable the Assessor to release UPP owner Social Security numbers to the Tax Collector, who would be required to maintain the confidentiality of this information.

Clearance Unit

The Clearance Unit of the Investigations Division processes Business Registration applications. The Unit performs a function that is very close to the delinquent account consolidation that was discussed above. Although the Clearance Unit does not maintain a database of delinquent UPP and BTS accounts, the staff of the unit check in both systems to verify that the Registration applicant does not owe taxes or fees to the City. Annual Registration Certificates are withheld pending payment of delinquent bills. The only time when a taxpayer might receive a consolidated bill for both delinquent UPP and business taxes is when the Clearance Unit sends them a bill. The current work of the Clearance Unit demonstrates that, even without a network between the UPP and the BTS databases (which would greatly speed the process), it is possible to identify parallel accounts in the two systems.

The Clearance Unit should be part of the proposed consolidated Accounting Division, because its task is essentially an accounting task. There should be considerable opportunity to make efficient use of staff time by combining clearance efforts with delinquent account consolidation efforts.

Accounts Payable, Bank Account Reconciliation and Budget Analysis

Although examination of the operations of the Treasurer's Office was beyond the scope of this management audit, the recommendation of the Tax Collector's TQM Task Force to consolidate accounts payable, bank account reconciliation and budget analysis functions of the Tax Collector with those of the Treasurer is sensible.

Assessor's Reassessments to Property Tax Rolls

Although we do not recommend consolidation of Secured Property Tax accounting in the proposed Accounting Division, because of the complex relationship between the Tax Collector's database and those of the Assessor and Controller, there is one area of Property Tax accounting that is highly inefficient. The Tax Collector currently employs a staff of five Account Clerks and a supervisor to issue refunds and respond to inquiries from taxpayers about over- or underpayments of Property Tax. One reason for the high volume of refunds is that there is a delay between the time the property owner requests a reassessment and the time the reassessment is completed and posted to the Assessor's Tax Rolls. As a result, many taxpayers submit a check based on the reassessed value, but the Tax Collector has to return the check, request a check based on the original value of the property, and then process a refund to the taxpayer when the reassessed value finally shows up on the tax rolls. This is a substantial waste of Tax Collector staff time, and clearly costs the City the goodwill of effected taxpayers.

The Tax Collector advised us that the Assessor's Office is presently taking steps to improve its automated systems so that the tax rolls can be updated more promptly. The Tax Collector should closely monitor the progress of these efforts, and continue to support their implementation.

SUMMARY

Accounting and data entry functions are currently distributed throughout the Divisions of the Tax Collector's Office. Efficiency improvements that will improve collections can best be implemented by establishing a consolidated Accounting Division, as recommended by the Tax Collector's Total Quality Management (TQM) Task Force Charlie.

Collections efforts are hampered by the nearly four month process of entering Business Tax Statements to the BTS system, which will likely be shortened by the planned introduction of scanners for statement entry. An Accounting Division would provide an environment in which performance goals for statement entry could be monitored and enforced.

The fragmented check control process takes time away from revenue producing activities. Business Tax, License, Fees and Unsecured Personal Property Tax (UPP) check control should be centralized after the centralization of accounting is complete, in accordance with the recommendations of Task Force Charlie.

Tracking of delinquent accounts can be improved in several ways. Use of the BTS system should be maximized to facilitate calculation of interest and penalties, eliminating manual calculation by multiple Divisions. The proposed Accounting Division should cross-check delinquent UPP and Business Tax Accounts, so that taxpayers can be notified of both delinquencies simultaneously, and Collections Officers can pursue full payment.

The Assessor's Office is responsible for substantial delays in posting reassessments in property values to the Tax Rolls. As a result, the Tax Collector has to process numerous check returns and subsequent refunds, as taxpayers submit initial payments for reassessed amounts that cannot be accepted by the Tax Collector until they are reflected on the Tax Rolls. The Tax Collector should closely monitor and support the progress of automation efforts in the Assessor's Office.

RECOMMENDATIONS

The Tax Collector should:

1. Establish a separate Accounting Division, in order to centralize account maintenance and delinquency billing. This consolidation will provide clear lines of responsibility for accounting tasks so that standards of performance can be set and actual performance can be compared with these standards. The Accounting Division should handle (1) statement entry for Business Taxes; (2) maintenance of payment and collections records on delinquent accounts; (3) reconciliation of Business Tax, Business Registration, License, and Unsecured Personal Property account data with FAMIS; (4) check control and bad check processing for all taxes except Secured Personal Property Tax; (5) cross-checking of delinquent accounts to identify all taxes due, and preparation of consolidated delinquent bills; and (6) clearance of Business Registration applications.

2. Use the Accounting Total Quality Management (TQM) implementation group to plan the phased implementation of consolidated accounting, as recommended above.

3. Implement a goal of processing all Business Tax statements received by the February 28 filing deadline within 30 working days, or by approximately April 15 of each year. Dedicate two clerical staff to full time scanning of statements during this 60 day period, and four clerical staff to full time data entry of complex statements, in order to achieve entry of all statements by April 15.

4. Hire the full roster of authorized accounting employees. In particular, hire a Head Accountant. Charge this person with supervising statement entry data and mailing initial Business Tax delinquency notices to businesses by no later than May 1 of each year.

5. Make a high priority request to the Controller's Information Services Division (ISD) to complete programming of screens to permit the Business Tax System (BTS) to handle all records of collections activities on delinquent Business Tax accounts, including penalties and interest, installment payment arrangements, records of notification sent to delinquent taxpayers, liens and seizures of accounts, and legal actions.

6. Eliminate separate record-keeping by Divisions with collections responsibilities. Require collections personnel to report all payment arrangements and payment receipts to the Accounting Division for entry to the system.

7. Work with the Assessor and the City's elected State representatives to effect any needed changes to the State Revenue and Taxation Code, to enable the Assessor to release unsecured personal property owners' Social Security numbers to the Tax Collector, who would be required to maintain the confidentiality of this information. This would enable the Tax Collector to cross-check delinquent UPP accounts with delinquent business tax accounts to improve the efficiency and effectiveness of collection activities.

8. Continue to support and encourage efforts to automate the Assessor's Office procedures for entering reassessment data to the Property Tax Rolls.

COSTS/BENEFITS

Transferring check control activities from revenue producing Auditors and Investigators would result in an estimated $276,641 annually in increased collections. In general, consolidating accounting and implementing the efficiency improvements recommended here would improve collections activities, and increase revenues, by permitting earlier notification of delinquent taxpayers, and providing collections staff with more complete and accurate information about total taxpayer liabilities.

SECTION I.2: AUTOMATION

The Tax Collector has invested more than $3.75 million in new automated systems for maintaining taxpayer account data over the past three years. This investment is largely going to waste, because staff have not been trained to take advantage of the improvements. Available training is too brief, too narrow in scope and provides no follow-up to ensure that staff are able to use the systems they need at maximum efficiency. The Tax Collector should enhance training, and then require managers to evaluate staff's mastery of systems related to their jobs.

The Administration Division should convene and consult with internal user's groups to provide end-users with on-going information about the customer software developed by the Controller's Office for the Tax Collector's Office. The Division should provide clear procedures for communication of decisions related to automated systems to end-users in the Department.

The Tax Collector's Office and the Controller have restricted access for individual staff to the existing computer systems based on position duties. Many of the restrictions serve no useful security purpose, but prohibit staff from accomplishing tasks without assistance from other staff. The access restrictions keep staff ignorant of how their work effects others. Access rules should be revised to provide at least read-only access to improve efficiency.

The Tax Collector should also work towards linking the Business Tax System (BTS) with the Unsecured Personal Property Tax System (UPP), the database maintained by the Assessor, and the City's main financial accounting system, notwithstanding budgetary considerations and ordinance changes that might stress the Tax Collector's resources. Establishment of working system interfaces will improve collections, facilitate identification of unregistered businesses, and simplify taxpayer assistance.

The functions performed by the Tax Collector's Office require the maintenance and manipulation of large databases. Throughout the Office, the degree of automation is a crucial determinant of the quality and quantity of work that can be accomplished. We therefore examined the status of automation throughout the Tax Collector's Office as part of this management audit.

In order to identify the strengths and weaknesses of the Tax Collector's automated systems, we took the following steps:

- interviewed the Senior Administrative Analyst in the Administration Division, division managers and mid-level managers of units whose work involves database functions;

- interviewed end-users in the Tax Collector's Office about how they use the automated systems, and observed their work;

- examined the major systems used by the Tax Collector with staff of the Controller's Information Services Division (ISD), who developed the systems;

- reviewed discussions related to automation in the two Total Quality Management (TQM) reports that have been prepared by task forces within the office[1]; and

- reviewed the chapter on "External Interfaces," of the "Total Requirements Statement for the Business Taxes System."[2]

We found that the Tax Collector's Office has made significant recent progress toward the automation of tax collection and recordkeeping functions. However, we also found that the full benefits of these improvements are not being realized because line staff do not know how to make full use of the systems, do not have adequate knowledge of or access to related components of the systems, and have little input to or information about plans to alter the systems. We also found that the various databases are not linked, so staff (and, by extension, taxpayers) have to consult separate systems for information about a taxpayer's status related to every tax and fee collected by the City. The Tax Collector is aware of the need for linked databases, but has been prevented from implementing a linked system because of budgetary limitations, changes in tax ordinances and Assessor's Office policy changes related to database linkage.

---

[1]"Task Force Bravo: A Report on an Examination of Tax Payer Assistance in the Office of the Tax Collector of the City and County of San Francisco," October 5, 1994; and "Final Report and Recommendations of Task Force Charlie," January 20, 1995.

[2]"Outline Physical Design and Total Requirements Statement for the Business Taxes System," Volume Two, Chapter 5.2.6, "Design Unit 6 - External Interfaces," Office of Treasurer/Tax Collector, City and County of San Francisco, March, 1991.

This Section of our report does the following:

- provides an overview of the automated systems used by the Tax Collector's Office;
- specifies training needs, including system overview training, data analysis training and training follow-up;
- details communication problems related to automation, and proposes organizational and procedural solutions;
- examines the effect of limiting access to systems on the quality and quantity of work that can be done;
- proposes employee evaluation criteria related to use of automated systems;
- identifies systems linkages that would improve operations; and
- provides recommendations for more effective automation of the Tax Collector's Office.

AUTOMATION OF TAX COLLECTION FUNCTIONS

Over the past three years, the Tax Collector's Office has made considerable progress in installation of automated systems for tax collection and recordkeeping functions. With the assistance of ISD and an outside vendor, the Tax Collector's Office has implemented a new mainframe Business Tax System (BTS) and Unsecured Personal Property Tax History Files (part of the Unsecured Personal Property System, or UPP), and begun migration from a Wang mini-computer system to a Local Area Network (LAN).

Business Tax System (BTS)

The BTS program contains records of payers of Payroll and Gross Receipts Taxes, Business Registration fees, Hotel Tax, Parking Tax, as well as non-tax paying registered businesses. The system was installed in 1991, at which time historical records dating back to 1988 were entered to the database. As designed and in its current configuration, the Business Tax System has 110 to 115 on-line screens. The data includes information regarding the tax status, location, and ownership of businesses, and business owners, registered in the City. BTS provides the Tax Collector with the ability to track a taxpayer's status with respect to billings, payments, delinquencies, penalties and interest, address changes, and many other details, once annual Registration and Business Tax Statements have been entered into the system.

Selected members of the Tax Collector's staff and ISD spent two and one-half to three years designing, testing and implementing the BTS. Excluding the cost of the Business Tax Division's staff time (and related revenue losses) devoted to

developing the Business Tax System, $3,602,000 has been spent directly on its implementation. This includes $2.5 million for system implementation, $720,000 for releases 1A and 2, $164,000 for new development, $184,000 for implementing changes resulting from ordinances and $34,000 for implementing changes needed to conduct the Amnesty Program.[3]

The BTS program gives the Tax Collector the potential opportunity to conduct sophisticated analyses of business tax data. The system could be used in combination with the LAN to perform such tasks as selection of businesses to audit, and tracking of collection efforts to determine what methods are most effective and what accounts are most/least collectible. However, as of the writing of this report, little of this analysis potential has been tapped. In fact, as will be detailed, implementation of BTS has actually contributed to a decline in productivity in the Business Tax Division because (1) considerable staff time has been taken to document the system; (2) end-users find the many screens confusing and are uncomfortable with manipulating the data; (3) requests to ISD for changes or special adjustments meet with lengthy delays;[4] and (4) access to screens has been overly restricted.

Unsecured Personal Property (UPP) System

The UPP System contains records of taxpayers who own personal property (other than real estate) that is used in conducting business.[5] Like the BTS, the UPP system provides accounting functions to track the taxpayer's status with respect to billings, payments, delinquencies, address changes and many other details, with historical records dating back to 1990.

Implemented in 1992, the history portion of the UPP System replaced a manual system of hand written and calculated ledgers and card files to track payments made on delinquent tax obligations. Automation of this data enabled the Investigations Division to more easily and efficiently track Unsecured Personal Property Tax payments, and permitted the Property Tax Division to credit the General Fund for partial payments of Unsecured Personal Property Taxes, rather than holding such records in a suspense account indefinitely.

Development and installation of the UPP personal history tax files by the ISD cost a total of approximately $68,750. Unlike the BTS system, the UPP personal history tax files were installed with relatively little disruption to ongoing operations, and have already resulted in improved accounting practices.

---

[3] The costs detailed above do not include expenditures related to the use of the central computer (CPU costs), routine maintenance of the system or ongoing production support. Cost for such items are reflected in the annual operating budget for ISD and paid by the Tax Collector's Office as a charge-back.

[4] ISD responds to such requests in priority order established by the Tax Collector.

[5] The Assessor's Office maintains a separate database containing records of secured property tax accounts, chiefly relating to real estate.

Local Area Network

The Local Area Network, or LAN, is a Personal Computer (PC) based system containing PC applications such as Microsoft Word, EXCEL, and PARADOX. These applications are designed to allow the staff to run word processing, spreadsheet and data base applications from a computer located on their desk. Whereas the mainframe BTS and UPP systems are used to maintain detailed account databases, the LAN software is to be used for analysis and report preparation. Connection to the network also allows each staffperson to log-on to mainframe applications from any computer connected to the LAN. Through special requests, information from the two mainframe systems can be downloaded by ISD to the LAN and then queried and manipulated to produce special management reports.

The Tax Collector's Office is currently in the process of migrating from a Wang mini-computer system environment to this new LAN environment. As of the writing of this report, the Business Tax, Administration, Legal and Bureau of Delinquent Revenue Divisions have migrated to the new system. The remaining Divisions (Real Estate, Investigations and Licenses) will migrate to the new system after the Tax Collector's Office has completed its move from City Hall. The total cost of hardware and software for the LAN was approximately $85,670.

Migration to the LAN should eventually allow the Tax Collector's Office to automate tasks which are currently carried out manually. These tasks include the reconciliation of Real Estate files with Financial Accounting Management Information System (FAMIS) files,[6] and the reconciliation of the Unsecured Personal Property Tax Division's transactions with FAMIS and the Business Tax System (BTS) files and hand written ledgers kept for internal records. However, these tasks will only be automated when (1) the Tax Collector is able to obtain priority status for the necessary programming by ISD; and (2) staff is trained to plan and execute analysis based on a thorough knowledge of the mainframe databases and the software available on the LAN.

TRAINING IN USE OF AUTOMATED SYSTEMS

Automation needs and training requirements for the Tax Collector's Office staff are coordinated by the Administration Division. As of the writing of this report, the Administration Division has one MIS staff position. However, by FY 1995-96, the Tax Collector expects to have hired a second MIS and an MIS manager. Working with staff from ISD, these three positions will be responsible for organizing and coordinating training, administering LAN activities and implementing changes to existing systems. The Tax Collector should make full use of this augmented MIS staff to improve the understanding and efficient use of automated systems throughout the Tax Collector's Office.

---

[6]The Financial Accounting Management Information System (FAMIS) is the City's main financial accounting system. FAMIS is maintained by the Controller's Office.

Overall training on the mainframe applications available to the Tax Collector's Office currently is inadequate and ineffective. Consequently, the staff is unaware of: 1) the capabilities of the systems when used separately, or in conjunction with each other; 2) possibilities for creating specially designed screens to provide more appropriate information; and 3) the degree to which incorrectly or inconsistently keyed data impacts the operation and integrity of the system.

System Overview Training

The Budget Analyst's review of the use of automated systems available to the Tax Collector's staff revealed a pressing need for comprehensive training of all employees on the systems used and the relationships between those systems. Currently, staff is unaware of the inter-relationships between the data contained in sections of the systems they are responsible for maintaining and the data contained in sections maintained by other employees. Due to the fragmented nature of data entry and accounting (see Section I.1), staff is also unaware of the importance of maintaining a high degree of accuracy and the impact of erroneous data on various tasks performed by other staff members.

The problem is particularly acute for users of the BTS system. BTS training modules were designed to provide staff with instruction on the functionality of the original system with respect to specific job functions. However, the Business Tax Division staff needs additional training on the Business Tax System to: 1) provide context for the tasks they perform related to the updating and maintenance of the system, and the impact of those tasks on interconnected parts of the system; and 2) ensure that the system is used efficiently and to its fullest capabilities.

Based on directives from the Tax Collector, ISD tailored training on the BTS to specific job functions. For example, data entry staff were trained only on the correct entry of information to the specific screens they would use to accomplish their tasks. Auditors were trained to use the system to access the specific information they would use to conduct audits and access the screens which contained the information they needed. Except for higher level administrative staff, no one has an overall view of what the Business Tax System was designed to do, how it must be maintained to function properly, and the role each staff person plays in making sure the system is sound. This approach to training and access was based on the directives of a Security and Controls Committee composed of representatives from the Tax Collector and the Controller's Internal Audits Division. Restricting training to the specific areas of job responsibility has greatly limited the number of staff members that have a global view of the Business Tax System and its capabilities.

We encountered several instances of inefficiency that could have been avoided if staff had adequate training in the overall functions and capabilities of the systems. (1) Statement processing personnel and auditors assigned to input address changes use inconsistent abbreviations, which can unnecessarily complicate future account searches. In addition, a high error rate (we estimate up to 15 percent) is tolerated in address changes, even though this renders billing and collection extremely problematic (See Section I.1: Accounting and

Statements); (2) Data entry of filings under the Amnesty Program was delayed (for a variety of reasons, including programming delays at ISD), without addressing the resulting inability of the Clearance Unit to issue Business Registration Certificates to businesses that paid their annual Business Registration fees.

In order to broaden the staff's understanding of the automated systems, the Tax Collector should provide system overview training on the functionality of all systems used by staff. This will allow staff to view their work in a broader context and understand the inter-relationship between the tasks one individual performs and the tasks performed by other staff members.

The recommended training could be provided by the staff of ISD at a cost of $75 per hour. To be effective, the system overview training sessions should contain various classes of employees, (e.g. investigators, auditors, account clerks, data entry clerks, etc.) and should take place in a setting that allows staff to view and access various parts of the system. ISD recommends conducting eight-hour sessions with a maximum of 14 trainees per session. Training for the 126 staff members can be accomplished at a cost of $5,400 (9 sessions of 14 participants each times 8 hours @ $75/hour).

Data Analysis Training

In order to make full use of the capabilities of the new LAN, additional training must provide instruction on the ways in which data contained on BTS and UPP could be downloaded to a PC and then manipulated using PARADOX and EXCEL to create management reports and reconciliation records that are currently produced manually, if at all. For example, data on businesses that have not paid annual business registration fees could be queried by type of business and tracked to determine if greater enforcement efforts are needed for specific classes of businesses such as restaurants, dry cleaners or small printing shops.

This type of analysis can enhance the effectiveness of a wide variety of tasks performed throughout the Tax Collector's Office. However, analysis will only happen if those whose work would benefit from such information understand what the systems can do for them. This is particularly important because the staff of ISD does not provide individual technical assistance to the Tax Collector's line staff on a regular basis. (Instead, ISD provides assistance to certain members of the Tax Collector's staff, who are responsible for assisting other Tax Collector staff members.) Managers and analysts in the Tax Collector's office need the skills to enable them to develop precise programming requests with a minimum of assistance.

The efforts of the Business Tax Division to develop an audit selection program provide an example of the inadequacy of data analysis skills in the Office. Audit Unit staff worked with ISD to enumerate variables they considered relevant to audit selection. However, they initially neglected to weight the variables, so the audit selection program developed by ISD selected approximately 6,000 accounts,

rather than the 500 that the Chief Auditor felt could realistically be completed in a year. The program has since been refined to provide a more useful audit selection.

All staff are currently receiving introductory training on the LAN spreadsheet and database programs. The Tax Collector should build on this training with practical data analysis training. All management and analyst staff at the Tax Collector's Office, along with specific personnel who are responsible for the preparation of management reports, should receive training in data analysis to complement current training being implemented by the Tax Collector related to use of the LAN. Such training should cover not only the requisite computer software skills, but also basic rules of thumb related to data analysis. The Tax Collector's Office should carefully communicate the goals of this training to ISD, as ISD has not demonstrated consistent success in helping the Tax Collector's staff analyze data in the past. The training should involve two eight-hour sessions, with the first session used for instruction in general methods, and the second session devoted to analyzing cases brought by participants. If approximately one-third of the Tax Collector's staff (42 persons) received data analysis training in three groups of 14, the total cost of the training would be $3,600 (3 sessions of 14 participants each times 2 days times 8 hours @ $75/hour).

Training Follow-up

Training sessions at best provide a solid introduction to their subject. It is only when staff return to their daily tasks that the training is put to the test, and new questions inevitably arise. This is the point at which the Tax Collector's new MIS staff and Division managers should play a vital role in ensuring that staff make practical use of the available automated tools. Our investigation revealed, however, that no such follow-up is systematically provided.

The recent training of the staff of the Bureau of Delinquent Revenue on the LAN provided one day of instruction on the system and applications available. The basic training provided instruction on the use of Windows and an introduction to Microsoft Word. (Staff interested in more training on specific applications such as EXCEL and PARADOX must make individual requests for such training.) Management was aware that not all of the staff trained was comfortable using the applications after the training. Nevertheless, the only assistance provided to those staff members needing additional help came from other staff members in their section. This practice assumes (1) that there is at least one person doing each functional automated task who has a sound understanding of the system or program involved; and (2) that the staff who need help know what questions to ask. The latter assumption is even more problematic than the former. Only by having the experts observe the end-users at work can the Tax Collector ensure that inefficient practices will be corrected.

The lack of follow-up on training is also apparent with respect to the use of mainframe systems. During the Budget Analyst's review of the automated systems used by the Tax Collector's Office, Business Tax Division staff members were asked about features available on the system and the ability of the system to provide summary information on the delinquency status of a taxpayer. Staff

indicated that such information had to be compiled from several screens or from a transaction screen, and that accessing information was cumbersome. However, further investigation by the Budget Analyst revealed that a statement history and detail inquiry screen, designed by the Clearance Section of the Investigations Division, is available and that "hot key" and "toggle" capabilities have been installed within the system to increase access speed. If MIS staff regularly observed end-users at work, they could pinpoint such inefficient practices and correct them.

Once three full-time MIS positions are available, the Administration Division MIS staff should coordinate with Division managers to provide follow-up assistance for each Division that has recently been trained on the use of a new system.[7] This assistance should include physically observing staff members using the new system and providing instruction on the proper use, if required. In coordinating this type of follow-up to training, MIS staff will be better able to coordinate with the rest of the Administrative staff and ISD to improve and tailor training sessions to cover the topics of greatest concern to the staff. To the extent that Division managers are expert users of the automated systems, the managers could be asked to perform these one-on-one observations. These efforts should be supervised by MIS staff, who should be available as needed to assist managers in improving individual user skills.

COMMUNICATION BETWEEN AUTOMATION USERS AND DECISION MAKERS

During the original development of the automated systems, staff from various Tax Collector divisions had considerable input. However, our investigations reveal that MIS staff in the Administration Division rely almost exclusively on senior managers of the other Divisions in the Tax Collector's Office to be the conduit for on-going information related to automation. This practice detaches end-users from the process of making automation work for the Tax Collector's Office, and reinforces an organizational culture that resists automation.

We observed several examples of these communication problems. When planning the migration of the Business Tax Division from the existing WANG minicomputers to the LAN, Administration's MIS staff worked through senior managers to identify what software each employee should have and to explain how the change to the LAN would effect the Division. Because the needs of certain end-users were not clearly or effectively identified by and communicated through senior managers, it was necessary to carry out subsequent software installations. In addition, self-selection for training on various LAN applications, without assessment by knowledgeable MIS personnel, resulted in inadequate training on applications which would be used by some staff members, and training on

[7]Initially, observations should be completed for all staff using the BTS system as well, even though they received training when the system was installed in 1991, because there is ample evidence that many users are not knowledgeable about many features of the system and remain uncomfortable with use of the system.

applications which had no relevance to job related duties by others. The Administration Division reports that this experience led them to take a more direct approach in meeting with end-users of the LAN in the Bureau of Delinquent Revenue (BDR) prior to implementing that Division's migration to the LAN, resulting in a more successful transition.

Another example of inadequate involvement of end-users in automation planning is the process underway at the time this audit was written to implement on-line access to the Controller's accounting system, FAMIS, which is scheduled to start in July, 1995. FAMIS contains information that could be useful to several Divisions within the Tax Collector's Office, including accounting personnel who perform reconciliation of FAMIS reports to BTS and UPP reports, as well as investigators and personnel involved with identifying unregistered businesses, who could make use of City vendor information that is available on FAMIS. FAMIS is a large mainframe database system, and planners from ISD and the Tax Collector's Office will have to make many decisions regarding what portions of the system should be provided on-line to the Tax Collector's Office. It is important that the end-users of the system have input regarding the contents and configuration of the information that will be provided on-line. However, the ISD team responsible for developing the on-line FAMIS system meets only with senior management of the Tax Collector's Office. The information provided and the issues discussed at these meetings are not shared by management with the likely end-users of the on-line FAMIS.

A third example of the neglect of end-users in automation planning is the process of obtaining modifications to automated systems by the Controller's ISD. End-users can make requests to ISD through supervisors; ISD indicates that approximately 45 to 50 requests from the Tax Collector's Office are currently outstanding. However, the Tax Collector's requests must compete with requests from many departments for ISD assistance. The Tax Collector participates on a committee composed of representatives from the various departments that use ISD's services, where the requests are evaluated and prioritized. It is crucial for the Tax Collector's Office to conduct its own internal assessment and prioritization of automation requests, to ensure that the Tax Collector is fully informed of the consequences of delaying or canceling a request to ISD. Given the limited resources of ISD, there may in fact be cases where the Tax Collector should use outside programming assistance to avoid costly delays.

A case in point is the request for programming related to processing of the Amnesty Program applications on Paradox software, which was made to enable the Business Tax Division to manipulate and analyze the program results more effectively than if the application data was entered directly to the BTS system. The ISD programmer who was handling this project resigned midway through the task, in late 1994. ISD negotiated a new deadline with the Tax Collector for completing this program of the end of April, 1995, and ISD anticipates meeting this later deadline. This later deadline is problematic: April, 1995, is beyond the final deadline of the Amnesty Program application period. Delays in preparation of this program will have a ripple effect on the Division's ability to clear business registrations and to issue the delinquent tax determinations that are currently the

main collection tool for collection of unpaid business taxes. A well-managed internal automation prioritization process might have averted this problem or provided an alternative strategy for processing of the Amnesty applications.

MIS staff should establish user's groups for the BTS and UPP systems, as well as for LAN users. The Tax Collector used such groups extensively in the development of the BTS, and should revive this practice to ensure ongoing communication with the end-users. Participation in the user's groups should be composed primarily of representatives of end-users from a variety of job classifications and divisions -- not their supervisors. The Tax Collector, through the Administration Division's MIS staff, should employ the user's groups to help prioritize systems modifications and to help plan automation changes. The end-user representatives should, in turn, be responsible for communicating information about the systems to their co-workers.

ACCESS LIMITATIONS

A Security and Control Committee, consisting of representatives from the Tax Collector and the Controller's Internal Audits Division, has restricted access to the existing computer systems based on job duties, with lower paid classifications denied access to screens containing confidential information. One of the problems with structuring security and access in this manner is seen in the earlier discussion on system overview training. Limiting access to the system, while important in some cases, prevents the line staff from developing a global understanding of the systems they use.

A still more unfortunate consequence of designing a security policy based on job duties (which translates to civil service classification) is that the access restrictions have led to routine misallocation of resources. Professional staff, including auditors, must perform essentially clerical functions, because clerical staff cannot access all of the computer screens they would need to correct non-financial account data. The Administration Division and senior managers need to reevaluate automated system security policy. Security and confidentiality are extremely important in the Tax Collector's Office, but these concerns should be addressed without sacrificing efficiency. All employees should be required to sign confidentiality statements. The Administration Division should work with the Human Resources Department to develop brief training modules on confidentiality issues for line staff and supervisors. Genuine security will be further enhanced by consolidating the accounting/statement entry functions (as recommended in Section I.1), and the collection functions (as recommended in Section IV.2), which will provide more checks and balances than under the current organization of the Tax Collector's Office. The fact that an employee occupies a lower-paid classification does not, by definition, render them less trustworthy than a higher-paid employee. Managers need to start by identifying all of the screens that each staff person should be able to access in order to maintain an appropriate distribution of tasks.

Full access to any screen can be provided without any programming changes to the system, at no cost. ISD reports that the system could easily reflect that the

individual with a specific identification code was granted full access to the information contained on a particular screen. ISD would simply need to get instructions from the Tax Collector's Office to change the status of a particular staff member with a specific identification code to grant such access.

In some cases, staff only need to view screens in order to obtain information; they do not need to be able to modify the screens. Providing "read-only" access in such cases would preserve security restrictions while permitting staff to get their job done. For example, staff of the Clearance Unit in the Investigations Division need to review BTS, UPP and licensing records prior to issuing Business Registration Certificates. They are not able to access all of the BTS screens they need, so they must refer business tax queries to auditors. This is a waste of revenue-producing auditor time, and adds unnecessary steps to the Clearance Unit's workload.

EVALUATION OF PERSONNEL ON AUTOMATION SKILLS

Use of automated systems is essential to the operations of the Tax Collector's Office. Once the recommendations discussed above regarding automation training, establishment of user groups and revision of screen access policies have been implemented, the Tax Collector should require all employees to learn how to operate the systems they need to use at maximum efficiency. All personnel evaluations should include an appraisal of the employee's mastery of the relevant automated systems. Failure to learn the system well enough to use it to its full potential should not be tolerated; and efforts on the part of employees to improve the implementation of the automated systems should be recognized.

The Administration Division should establish standards for use in personnel evaluation regarding work practices and work products that will: 1) compel staff to use the new technologies that have been provided; 2) require the staff to develop a minimum level of competence with regard to operating and understanding all of the computer systems used to carry out the functions of the office; and 3) encourage staff to seek continuing training that allows them to develop their computer skills and operate in an efficient manner.

For example, if reconciliation of accounting data or preparation of statistical reports can be accomplished through the automated systems, the work product standards should specify that the reconciliation or the report must be accomplished in this fashion, rather than manually.

Unlinked Data Bases and Systems

The data bases used by the Tax Collector's Office are all housed on main frame computer systems. Even though these data bases are all main frame systems, they are not capable of communicating with each other, and the information contained on each system must be updated separately.

There are several areas where service and efficiency could be improved by developing interfaces. These areas include Customer Service, Collections, Accounting/Statement Entry, and Business Identification:

- Interfacing the existing systems would facilitate consolidated customer service as recommended in Section I.3. Trained service representatives could provide one-stop assistance to taxpayers about all of their tax obligations to the City, if it was possible to access all account data for a taxpayer and produce a single report.

- Collections would be facilitated by making it easier for the Clearance Unit to check on taxes owed prior to issuing Business Registration Certificates. In addition, collections personnel would have a simple way to determine whether a taxpayer who is delinquent on one type of tax or fee also owes the City another type of payment, so that collections procedures could address the taxpayer's full obligations to the City. Once all outstanding taxes had been paid, linking the systems would allow a global edit on the data so that all information in all of the data bases is updated at the same time.

- Accounting/Statement Entry could save significant amounts of time through use of an interface with FAMIS, the City's main financial system. An interface with FAMIS would enable staff to load information to a system, such as the Business Tax System, and get that information to post to FAMIS, eliminating the need for additional data entry and some manual verifications of transactions. Linking all of the Tax Collector's systems would allow some global edits of information that is common to all of the systems.

- On-line access to the Assessor's data or the Recorder's data about property ownership in commercially zoned areas could be an effective tool for identifying businesses that have not registered with the City.

In order to develop such interfaces, ISD and the Tax Collector's staff would have to identify or develop a common piece of data that is contained in each database and could be used as the key data field for identifying an account. A simple account identification number would be a social security number; however, changes in State legislation would be necessary to allow the Assessor to release social security numbers to the Tax Collector. In addition to identifying the common piece of data, standard data entry procedures would need to be in place.

The Tax Collector has recognized the need for system interfaces for some time. Specifications for the BTS system describe goals for "external interfaces" that are similar to those described here. However, these changes have been delayed due to reductions in the Tax Collector's budget which have delayed improvements to the Tax Collector's computer system and reduced staff, policy changes on the part of the Assessor, and frequent changes in legislation that have put a strain on the Tax Collector's existing resources. Given the current gap between automation system capabilities and staff's ability to take advantage of them, the interfaces discussed in this section should be viewed as long-term goals for the Tax Collector's Office. In the short-run, the Tax Collector's automation priorities

should be to: 1) implement training improvements; 2) improve communications with respect to automation needs, plans, and modifications;3) provide access to systems that will allow the staff to make full use of existing computer resources; and 4) assess mastery of automated systems in the context of personnel evaluation. Once these four improvements have been accomplished, details regarding interface programming requirements, modifications to existing data bases and costs for creating the appropriate interfaces should be developed.

SUMMARY

The Tax Collector has invested more than $3.75 million in new automated systems for maintaining taxpayer account data over the past three years. This investment is largely going to waste, because staff have not been trained to take advantage of the improvements. Available training is too brief, too narrow in scope and provides no follow-up to ensure that staff are able to use the systems they need at maximum efficiency. The Tax Collector should enhance training, and then require managers to evaluate staff's mastery of systems related to their jobs.

The Administration Division should convene and consult with internal user's groups to provide end-users with on-going information about the customer software developed by the Controller's Office for the Tax Collector's Office. The Division should provide clear procedures for communication of decisions related to automated systems to end-users in the Department.

The Tax Collector's Office and the Controller have restricted access for individual staff to the existing computer systems based on position duties. Many of the restrictions serve no useful security purpose, but prohibit staff from accomplishing tasks without assistance from other staff. The access restrictions keep staff ignorant of how their work effects others. Access rules should be revised to provide at least read-only access to improve efficiency.

The Tax Collector should also work towards linking the Business Tax System (BTS) with the Unsecured Personal Property Tax System (UPP), the database maintained by the Assessor, and the City's main financial accounting system, notwithstanding budgetary considerations and ordinance changes that might stress the Tax Collector's resources. Establishment of working system interfaces will improve collections, facilitate identification of unregistered businesses, and simplify taxpayer assistance.

RECOMMENDATIONS

The Administration Division should:

1. Obtain ISD assistance to provide all staff members with system-overview training on the inter-relationships between different functions of the automated computer systems.

2. Provide all personnel who are responsible for the preparation or analysis of management reports with training in data analysis using the software available on the LAN. Such training should cover not only the requisite computer software skills, but also basic rules of thumb related to data analysis.

3. Require Management Information System (MIS) staff to coordinate with Division managers in providing follow-up assistance for each Division that has recently been trained on the use of a new system. This assistance should include physically observing staff members using the new system and providing instruction on the proper use, if required.

4. Establish user's groups for the BTS and UPP systems, as well as for LAN users. Membership should be composed primarily of end-users of the systems. The MIS staff should employ the user's groups to help the Tax Collector prioritize systems modifications and to help plan automation changes, as well as to communicate information about the systems to co-workers.

5. Re-evaluate automated system security policy, to avoid sacrificing efficiency unnecessarily. Identify all screens that each staff person should be able to access in order to maintain an appropriate distribution of tasks with the Office, and obtain access revisions as needed from ISD. If necessary, implement alternative security measures including requiring employees to sign confidentiality statements, and working with the Human Resources Department to develop brief training modules on confidentiality issues for line staff.

6. Re-program the BTS system (and others, if necessary) to permit read-only access to specified screens for specified employees.

7. Establish standards for use in personnel evaluation regarding work practices and work products that will: 1) compel staff to use the new technologies that have been provided; 2) require the staff to develop a minimum level of competence with regard to operating and understanding all of the computer systems used to carry out the functions of the office; and 3) encourage staff to seek continuing training that allows them to develop their computer skills and operate in an efficient manner.

8. Continue to work with ISD to develop interface networks that will link the existing systems and ultimately allow an interface with FAMIS and the Assessor's database.

COSTS/BENEFITS

The cost of providing one-time system-overview training to all staff of the Tax Collector's Office would be approximately $5,400. The cost of providing data analysis training to staff who prepare or analyze management reports would be approximately $3,600. The cost of re-programming the BTS system to permit selected read-only access to screens should be determined by negotiation with ISD or by competitive bid.

The benefits of improving automation training, establishing automation user's groups, improving access to databases and evaluating staff's mastery of automated systems will be significant long-term productivity gains and improved ability to collect revenues due the City.

SECTION I.3: TAXPAYER ASSISTANCE

The Tax Collector's Office provides assistance to taxpayers separately in the Property Tax, Business Tax and Licensing Divisions. Most staffing for taxpayer assistance is provided by rotating staff who perform other functions within their respective Divisions. Problems include inadequate staffing of telephones, excessive transfers of taxpayers from division to division, provision of incorrect information, long lines, and communication problems due to language differences.

The Tax Collector is taking constructive steps to remedy these problems through a Single Point of Contact (SPOC) desk to direct taxpayers to the correct division, as well as through a Total Quality Management (TQM) task force ("Task Force Bravo"), which issued a report on taxpayer assistance in October of 1994 recommending the establishment of a consolidated taxpayer assistance group. Task Force Bravo also recommended that the Service Representatives staffing taxpayer assistance receive telephone and customer service training, that networks between computer systems carrying tax data be established, and that InfoCal stations and self-service VCRs with multi-language video instructions be provided in the taxpayer assistance area. We endorse the Task Force recommendations.

Several of the recommendations presented in other sections of this management audit will, if implemented, help provide Service Representatives quick access to accurate information, including: (1) providing employees with access to all computer screens they might need and training in what all systems can provide; (2) creation of a centralized Accounting Unit; (3) consolidation of license fee billing with Business Registration and Property Tax bills; and (4) providing more realistic tax determinations to delinquent business taxpayers. Progress in improving taxpayer assistance should be monitored through user surveys and evaluation of service quality in the Tax Collector's Annual Report.

We examined the Tax Collector's arrangements for providing in-person and telephone assistance to taxpayers, through direct observation, review of the Tax Collector's own internal TQM analysis of taxpayer assistance[1], and consultation with a representative of the Citizen's Assistance Unit of the Mayor's Office of Business and Community Services.

The quality of customer service in the Tax Collector's Office is more important to the City than might at first be surmised. Although the Tax Collector's Office represents an obligation to citizens, rather than a service to be enjoyed by them, a citizen's ability to obtain efficient, accurate assistance on local tax matters can have a direct impact on the level of voluntary compliance with tax regulations. In other words, the City can bring in more revenue if it is easy and relatively pleasant for taxpayers to conduct business with the Tax Collector's Office.

We found that the Tax Collector is aware of the serious shortcomings of current taxpayer assistance activities, and has given improvement of these activities a high priority. Problem areas concern communication with taxpayers, access to information within the department, and fragmented, rotational staffing that undermines accountability and efficiency. The recommendations of Task Force Bravo for establishment of a consolidated Taxpayer Assistance Unit staffed by trained Service Representatives address these issues in a constructive and practical manner. However, the full benefits of these proposed changes will only be realized when the Tax Collector's Office improves the underlying operations that are necessary to provide Service Representatives with quick access to accurate information.

This Section of our report includes the following:

- A description of the existing arrangements for providing taxpayer assistance, and the types of assistance requested by taxpayers.
- An overview of the types of complaints received from taxpayers regarding taxpayer assistance, and the problems identified by Task Force Bravo.
- A summary and analysis of the Task Force Bravo proposals for improving taxpayer assistance
- An analysis of how implementation of specific departmental changes recommended in earlier sections of this management audit will improve taxpayer assistance.
- A discussion of the need to obtain user feedback and perform progress evaluation on the taxpayer assistance function.
- Recommendations for improved taxpayer assistance.

[1]"Task Force Bravo: A Report on an Examination of Tax Payer Assistance in the Office of the Tax Collector of the City and County of San Francisco," October 5, 1994.

BACKGROUND

The Tax Collector's Office answers citizens' questions both in-person and over the telephone. The Tax Collector recognizes the importance of providing high quality customer service, and in November, 1993, established a Single Point of Contact (SPOC) desk. Taxpayers with questions go first to the SPOC desk. SPOC desk personnel then identify the appropriate division of the Tax Collector's Office to respond to the question, and direct the taxpayer to that division. Separate units, supervised by the respective functional divisions of the Tax Collector's Office, handle Property Tax, Business Tax/Registration, and Business License inquiries. The customer service workload in each Division fluctuates on a fairly predictable schedule during the course of the year, with the heaviest staffing needs during the month prior to the specific tax's due date, and during the month following the mailing of delinquent tax notices.

Many customer services personnel are not dedicated to providing customer service information, but rather are rotated to this function from other jobs within their Division. For example, the Business Tax taxpayer assistance desk has two full time clerks (including a temporary clerk), but relies on the Statement Processing Unit of the Business Tax Division to provide another one or two clerks to complete the staffing of in-person taxpayer assistance on an as-needed basis. The Audit Unit of the Business Tax Division handles telephone inquiries and provides technical backup for the clerks. The auditors have a rotating schedule under which each one typically spends one day per week on customer service duties. License Division personnel spend 1.5 to two hours each per day at the counter answering in-person inquiries; telephone calls ring at all desks and are answered by the first available employee. The Property Tax Division has one dedicated customer service representative who provides in-person service and answers general telephone inquiries. In addition, each assessed parcel is assigned to an individual employee; a customer may enter his or her block and lot number in the automated telephone system and be connected automatically with the employee who is responsible for his or her parcel.

Most property tax customer service is provided by the Assessor's Office, because the Assessor's Office is responsible for determining the amount of property taxes due and auditing property taxpayer accounts. However, many taxpayers initially contact the Tax Collector's Office with property tax questions because it is the Tax Collector's Office that sends the property tax bills and receives the payments. At the property tax customer service desk a taxpayer can look up the block and lot number of the specific parcel of property to locate the tax bill. However, in order to change the amount of the assessed taxes, the mailing address or other changes, the taxpayer must directly contact the Assessor's Office. The property tax taxpayer assistance desk in the Tax Collector's Office sees an average of 40 persons per day, except during the two weeks prior to and after the property tax due dates of December 10 and April 10, when the average increases to 400 taxpayers per day.

They receive approximately 100 telephone inquiries per day most of the year, but up to 1,000 during the property tax season.[2]

Taxpayer assistance needs regarding business registration and taxes usually involve questions about the correct way to fill out the Annual Business Tax Statement, how to register new businesses, and how to calculate the amount of taxes due. The heaviest traffic occurs in February, prior to the February 28 due date for filing the Business and Payroll Tax Statement; in October, prior to the October 31 deadline for filing and paying Business Registration Fees; and in December or January, following the mailing of the Statements of Account. Because new businesses register throughout the year, a constant flow of approximately 50 visitors and 230 telephone calls per day must be fielded by taxpayer assistance staff during non-peak periods of the year. At peak times, up to 200 taxpayers may seek assistance at the business tax service desks. Telephone calls at such times may exceed 2,000 per day, and far exceed the capacity of the telephone system and staff.

In regard to the License Division, customers may visit the Tax Collector's Office in person to make their payments. Also, taxicab drivers must come to the Tax Collector's Office in person to receive their picture identification. Telephone inquiries might include questions regarding the amount of the fee or the due date. Questions pertaining to the permit itself are referred back to the user departments. The License Division was unable to provide estimates regarding the number of in-person or telephone inquiries. However, during peak season, such as the period before taxicab licenses are due, License Division employees spend four to five hours per day manning the counter, rather than the off-peak 1.5 to two hours.

TAXPAYER ASSISTANCE PROBLEMS

An internal TQM task force established by the Tax Collector to examine the taxpayer assistance function identified the following perceived problems related to telephone customer service: (1) Telephones are frequently permitted to ring without answer; (2) Callers are put on hold for long periods of time; (3) After repeated attempts to call, callers get only a busy signal and end up coming to the Tax Collector's office in person; and (4) When telephones are answered, the taxpayer is sometimes transferred repeatedly among the sections before getting actual assistance; incorrectly referred to an outside agency; or given the wrong information.

The task force described the following shortcomings related to in-person customer services: (1) In person, taxpayers are frequently referred from section to section within the Department; (2) Taxpayers stand in line for long periods to discover that they are in the wrong line; (3) Taxpayers experience confusion and difficulty

---

[2]The number of inquiries recorded here are based on verbal information from the Tax Collector's Office. The Tax Collector's Office does not count the number of inquiries per day, and the Budget Analyst did not perform an independent assessment of the number of inquiries.

communicating because of language differences and the fact that the taxpayer has not provided his own translator; and (4) Taxpayers are unable to communicate with the Tax Collector's employee because either the taxpayer cannot convey his/her needs in English; the taxpayer is angry to begin with and cultural differences come into play; or the employee responds inappropriately to the taxpayer.

The Citizen's Assistance Unit of the Mayor's Office of Business and Community Services receives complaints from taxpayers regarding their inability to contact the Tax Collector's Office by telephone.

Our own observations showed that the rotational staffing of taxpayer assistance is disruptive and bad for morale. Staff view taxpayer assistance as a distraction from their work, rather than as an important function requiring special skills and knowledge.

TASK FORCE PROPOSALS

The Tax Collector's task force made several proposals for short-term and long-term improvements to customer services. The major proposals are summarized as follows:

- Establish a "service representative" unit, drawing ten experienced persons from existing sections who would work on customer service full time. Select highly motivated staff who could be trained to be generalists, with regular rotation among the customer service tasks. Ideally, develop a Civil Service classification for the Service Representatives, at a rate of compensation at least equal to a 1630 Account Clerk ($40,500 including salary and benefits). (Implementation of this recommendation will take time, due to Civil Service regulations.)

- Establish a consolidated customer service area, with seven windows utilizing flexible signage, so that the number of windows devoted to a particular tax or fee could be adjusted depending upon demand. Rotate staff between the windows and two to three telephone positions.

- Improve traffic flow with a number system and or a rope system such as is used in banks.

- Provide the Service Representatives with telephone training and personal contact training, particularly in dealing with difficult clients and with individuals from diverse cultures.

- Develop a centralized database for all information maintained by the Tax Collector, and eventually obtain access to relevant information maintained by other City departments.

- Install two InfoCal work stations in the Tax Collector's Office, with specific data relating to San Francisco taxes, in addition to the State of California information provided in all such workstations.

- Provide self-service VCRs with videos in various languages providing instruction in how to fill out Tax Collector forms.

- Install videophone technology to enable the Service Representatives to link specialist staff outside the customer service area in face to face contact with taxpayers without calling the staff away from their files and reference materials.

- Allow some employees to "telecommute" -- answer customer service telephones from their homes -- in order to provide telephone assistance prior to 8 a.m. and after 5 p.m.

As of the writing of this report, an experienced Account Clerk from the Business Tax Division had been assigned to coordinate Business Tax assistance, in an effort to provide more consistent service. In addition, a group of eight volunteers from various Divisions were participating in a pilot program of cross training, to provide them with an understanding of the full functions of the Tax Collector's Office. The Task Force Bravo facilitator advised the Budget Analyst that these steps were being taken as a first step towards implementation of the Task Force's recommendations, although no final decisions had been made regarding establishment of a separate, consolidated Taxpayer Assistance Unit.

While some of the task force proposals, such as installation of videophone technology and allowing employees to telecommute, require further consideration, we strongly endorse the general concept of consolidating customer services into a single unit, staffed year-round by a consistent group of employees trained to be generalists. This reorganization will improve customer service, both by simplifying access to assistance and by providing greater staff accountability. Although existing Divisions would lose personnel to staff the unit,[3] the current rotational staffing process is extremely disruptive to morale and ongoing operations. The customer service unit should provide a promotional opportunity for existing staff, with a job description that includes a requirement for mainframe and local area network computer competency.

Providing video or written instructions in key languages at self-service VCRs in the customer service unit area is also a practical idea that could improve the efficiency and quality of customer service a cost of approximately $10,000. The Tax Collector estimates that the cost of two InfoCal work stations and video hardware would be approximately $42,000. Software with instructional information in selected languages could be obtained for up to an estimated $40,000. Therefore, the total estimated costs of providing two self-service work stations could cost up to $92,000 of one-time expenses.

---

[3]As stated in the Introduction, the question of whether or not the overall staff of the Tax Collector's Office should be increased or reduced (in this case, to replace staff who transfer from other Divisions to the customer service unit) can only be answered after the reorganizations proposed here have been implemented.

DEPARTMENTAL CHANGES TO IMPROVE TAXPAYER ASSISTANCE

Establishment of a consolidated Taxpayer Assistance Division and implementation of the other task force recommendations will produce a marked improvement in the quality of service citizens receive at the Tax Collector's Office. The full benefits of these proposed changes, however, will only be realized when the Tax Collector's Office improves the underlying operations that are necessary to provide Service Representatives with quick access to accurate information. Several of the recommendations presented in earlier sections of this management audit will, if implemented, improve the Tax Collector's ability to assist taxpayers:

- As noted by the Bravo Task Force, development of computer networks that will link the Business Tax System (BTS) database with the Unsecured Personal Property Tax database (UPP), as well as with the Assessor's Real Estate database and FAMIS, will allow more taxpayers to obtain one-stop assistance. Even before the systems can be linked, Service Representatives should be trained and authorized to access information on all systems. (See recommendations in Section I.2 on Automation.)

- Creation of a centralized Accounting Unit will reduce the number of specialists within the Department who might have to be consulted to resolve a question about the status of a taxpayer's account. If all servicing of accounts -- including time payments and audit deficiency payments -- is handled centrally, identification and processing of "problem checks" should proceed more smoothly. Thus, taxpayer accounts would be credited more quickly and accurately, eliminating the need for some taxpayers to obtain assistance and ensuring that others receive up-to-date information without having to talk to more than one or two staff persons. (Implementation of this recommendation would be facilitated by State legislation to allow the Assessor to release social security numbers to the Tax Collector.) (See Section I.1 on Accounting and Statements.)

- Consolidation of license fee billing with Business Registration and Property Tax bills (as appropriate) will reduce bookkeeping work for taxpayers and allow those requiring assistance to attend to license fees and tax bills simultaneously. The consolidated tax bills will also facilitate the clearance of Business Registration Certificates. (See Section II.1 on Licensing.)

- Changing the method of calculating Business Tax determinations to provide delinquent taxpayers with a more realistic estimate of taxes owed will reduce taxpayer confusion. (See Section IV.1 on Delinquent Payment Process.)

USER FEEDBACK AND PROGRESS EVALUATION

As the Tax Collector makes improvements to the Taxpayer Assistance function, it will be important to monitor the success of the program. In addition to tracking objective measures such as average waiting time, changes in the type of assistance requests received and usage of written or video assistance materials, the Taxpayer Assistance Unit should obtain subjective input from taxpayers who use the services.

The unit should develop a brief user satisfaction survey, to ascertain (1) the type of assistance requested; (2) whether the inquiry was in-person or by telephone; (3) rating the level of courtesy shown by the Service Representative; (4) rating the efficiency and helpfulness of the Service Representative; (5) soliciting feedback on whether particular assistance tools (such as translated instructions) were helpful; and (6) asking the open-ended question, "How can we improve the quality of our service in the future?"

The survey could be mailed to a portion -- perhaps 5 percent -- of taxpayers who request assistance, with a postage-paid, self-addressed return envelope. (This would necessitate keeping a record of the name and address of tax assistance recipients.) Alternatively, the intake clerk could provide all taxpayers who visit the office in person with the survey and request that they complete it and drop it in a box as they leave. This method of survey implementation has the advantage that the name of the Service Representative could be written on the survey by the intake clerk, so that surveys could be used for personnel evaluation. Mail (or telephone) surveys would still be required to assess user satisfaction with telephone assistance.

The Administration Division should periodically evaluate the surveys (and the objective factors mentioned above), and discuss the results with the Taxpayer Assistance staff. Quality of service measures should be reported regularly in a section on Taxpayer Assistance in the Tax Collector's Annual Report. Implementation of such a survey would require additional on-going staff time from the Administration Division.

SUMMARY

The Tax Collector's Office provides assistance to taxpayers separately in the Property Tax, Business Tax and Licensing Divisions. Most staffing for taxpayer assistance is provided by rotating staff who perform other functions within their respective Divisions. Problems include inadequate staffing of telephones, excessive transfers of taxpayers from division to division, provision of incorrect information, long lines, and communication problems due to language differences.

The Tax Collector is taking constructive steps to remedy these problems through a Single Point of Contact (SPOC) desk to direct taxpayers to the correct division, as well as through a Total Quality Management (TQM) task force ("Task Force Bravo"), which issued a report on taxpayer assistance in October of 1994 recommending the establishment of a consolidated taxpayer assistance group. Task

Force Bravo also recommended that the Service Representatives staffing taxpayer assistance receive telephone and customer service training, that networks between computer systems carrying tax data be established, and that InfoCal stations and self-service VCRs with multi-language video instructions be provided in the taxpayer assistance area. We endorse the Task Force recommendations.

Several of the recommendations presented in other sections of this management audit will, if implemented, help provide Service Representatives quick access to accurate information, including: (1) providing employees with access to all computer screens they might need and training in what all systems can provide; (2) creation of a centralized Accounting Unit; (3) consolidation of license fee billing with Business Registration and Property Tax bills; and (4) providing more realistic tax determinations to delinquent business taxpayers. Progress in improving taxpayer assistance should be monitored through user surveys and evaluation of service quality in the Tax Collector's Annual Report.

RECOMMENDATIONS

The Tax Collector should:

1. Establish a Taxpayer Assistance Unit with full-time service representatives, as recommended by the Tax Collector's Task Force Bravo. The service representatives should be trained to use all relevant computer systems and given access to all screens that could provide information needed by taxpayers.

2. Immediately implement the task force recommendations regarding installation of self-service work stations for taxpayers, with basic information on how to complete tax forms provided in key languages.

3. Develop overview training in the BTS and UPP computer systems, and institute follow-up training, as recommended in Section I.2 on Automation. Continue to work with ISD to create networks between tax databases.

4. Implement recommendations made earlier in this management audit regarding centralization of accounting, consolidation of license fee billing with Business Registration and Property Tax billing, and changing tax estimation methodology to make business tax determinations more realistic.

The supervisor of the proposed new Taxpayer Assistance Unit should:

5. Develop and monitor measurements of quality of service to taxpayers, including wait time, use of self-service facilities, etc.

6. Implement, on an on-going basis, a brief user survey that asks for open-ended suggestions about how the Tax Collector could improve service to taxpayers.

7. Evaluate the service measures and the survey results. Discuss the results and means for improvement regularly with the staff of the Taxpayer Assistance Unit, and include a section reporting on Taxpayer Assistance in the Tax Collector's Annual Report.

COSTS/BENEFITS

It is impossible to measure the revenue effects of qualitative changes in the delivery of taxpayer assistance. However it is reasonable to assume that providing more efficient, accurate tax assistance will increase voluntary compliance with tax regulations, thereby increasing revenues. The estimated cost of providing two work stations with videotaped instruction translated into selected languages would cost up to $92,000 of one-time expenses.

SECTION II.1: LICENSING

The License Division prepares and mails a separate bill for each license, even if an individual or business owes more than one license fee. Also, the property tax bill and the business registration bill are prepared and mailed separately from licenses, so that most individuals and businesses receive more than one bill from the Tax Collector each year.

The Tax Collector should issue a consolidated property tax bill and a consolidated business registration bill. The Business Tax Division should allocate resources to administering license fees for individuals. Consolidating these bills will require various legislative changes as well as organizational changes.

This reallocation of licensing responsibilities would result in improved customer service and reduced administrative costs of $262,142 the first year and $487,622 in following years. Also, the Tax Collector can expect the collections rate for license fees to increase from, 90.1 percent to 97.19 percent for DPW and for the Rent Board. In addition, the City's business registration collection rate should improve. Such increased collections would have resulted in additional revenues of at least $371,805 in FY 1993-94. Combined savings and increased revenues would therefore equal $859,427 at current salary and license fee revenues.[1]

As part of this management audit, we reviewed the organization of the Tax Collector's Office. The purpose of this review was to determine whether divisions in the Tax Collector's Office, which may be operating efficiently on an individual level, could be administered more efficiently if its functions were dispersed or consolidated.

Our organizational review included identification of the activities of the License Division, and a comparison of those activities with the regular billing activities of the Property Tax Division and the Business Tax Division. We found that costs would be reduced, revenues increased, and customer service improved, if the

[1]Revenue estimates do not include increases or decreases in projected revenue that might result from legislative changes.

activities of the License Division were divided among the Property Tax Division and the Business Tax Division.[2]

This section of our report does the following:

- summarizes the activities of the License Division, including the purpose of the licenses in each user department;
- describes the benefits of eliminating the License Division and dispersing its activities, including issuing a consolidated property tax and business registration bill; and
- establishes specific recommendations for implementing this reorganization of activities.

BACKGROUND

The Tax Collector's Office functions as a department of revenue for San Francisco. One purpose of a department of revenue is to consolidate revenue collection for city departments: it is more efficient for the City to maintain a single system for regular billings than to establish a separate system, including equipment and personnel, for each user department. Toward that end, the License Division collects 145 license renewal fees for six departments: Public Works, Police, Fire, Public Health, Animal Care and Control, and the Rent Board.

In FY 1993-94, the License Division collected $9,428,251 in total license fee revenues, as detailed in the following table.

Table 4

License Revenue Collected by Tax Collector

FY 1993-94

	Fee	Penalty	Total
Public Works	$3,070,294	$34,299	$3,104,593
Police	741,096	12,573	753,669
Fire	410,341	4,878	415,219
Public Health	3,393,037	90,066	3,483,103
Animal Care and Control	71,287	152	71,439
Rent Board	1,579,997	20,231	1,600,228
TOTAL	$9,266,052	$162,199	$9,428,251

[2]We also found that dog licensing would be better administered by the Department of Animal Care and Control. We have included establishing a separate dog license program under the Department of Animal Care and Control as a separate section of this report (Section II.2).

The Tax Collector's License Division's activities include coordinating the mailing and printing of bills, processing payments (i.e., opening mail, entering data, forwarding checks for deposit), and responding to customer inquiries. The Division bills for each license separately, even if an individual or a business must obtain a number of licenses. The reason for this organization is that the Division has accepted incremental responsibility for collecting additional license fees over time, with no high level review of the changing needs of license administration.

The seven employees of the License Division (not including the Division manager) are assigned to administer specific licenses. For example, one employee coordinates collection of the Rent Stabilization and Arbitration fee. However, License Division employees assist in the administration of licenses outside of their assignments, according to the flow of work. Each license is administered separately from every other license; no consolidation of billing occurs.

The License Division's FY 1994-95 budget is $973,931.[3] The Division employs eight full-time employees, including the Division manager, at a cost of approximately $582,000 in permanent salaries and benefits, and temporary personnel, as necessary, at approximately $41,000. Other major expenditures include approximately $143,000 for filing liens against properties delinquent in the Rent Stabilization and Arbitration fee, as well as City Mail Services, at approximately $62,000, Controller's Data Processing, at about $56,000, and miscellaneous other overhead, equipment, reproduction and other costs totaling about $90,000.[4]

The Police Department, Fire Department, Department of Animal Care and Control, and the Health Department collect money, issue first-time licenses to applicants, and forward a copy of that license to the Tax Collector. In ensuing years, the user department performs an inspection, if necessary, and issues a permit, and the Tax Collector bills the business or individual an annual license renewal fee. The Tax Collector bills property owners for Department of Public Works and Rent Board fees directly from the Assessor's rolls, without participation by the departments.

The following paragraphs summarize the purpose and administration of licenses for which the Tax Collector collects fees, organized by department.

Department of Public Works

The License Division collects four license renewal fees for the Department of Public Works (DPW): party wall structure (i.e., two properties constructed on a single foundation, separated by a plaster wall), hotel, apartment house and condominium. The DPW performs inspections and issues permits to ensure compliance with the City's Building Code. The purpose of the Building Code is to ensure that San Francisco buildings have structural integrity and are safe for their occupants. The DPW identifies new buildings through its construction permit process.

---

[3] Of this, $175,034, or 18 percent, was offset by work order recoveries from the Rent Arbitration Board. The remaining $798,897, or 82 percent, was supported by the General Fund.

[4] The actual expenditure for the Controller's Data Processing in FY 1993-94 was $107,224, which was $45,351 more than the budgeted amount of $61,873.

Police Department

The License Division collects 80 license fees for the Police Department. According to the Police Department, these licenses are issued to businesses or persons engaging in activities that are, or were, identified as being difficult to regulate, and licensing was used to provide the City with tools to regulate those businesses. However, no explicit policy to this effect exists. The Police Department identifies businesses requiring Police licenses through normal patrol activities.

Examples of businesses from whom license fees are collected for the Police Department include Amusement Parks, Museums, Limousine Owners, Pushcart Peddlers, Poker Games, Circuses, Masked Balls, and Wild West Shows. Individuals as well as businesses may be required to obtain Police Department licenses. Individuals who must obtain Police Department licenses include Taxi Drivers (in Section III.4 of this report, we discuss the classification of taxi drivers as individuals versus businesses by the Tax Collector), escort service employees, tow car drivers and nude photographic models.

Fire Department

The License Division collects 23 annual license fees for the Fire Department. These licenses are issued to establishments that engage in activities that might cause fires, such as gasoline sales or spray painting. Permits issued by the Fire Department include Junk Yards, Parking Garages and Parking Lots, Movie Theaters, and Service Stations.

In most cases, businesses requiring licenses are easy to identify, either because few businesses perform the activity for which a license is issued, or because ownership and location of these businesses is relatively static, or both. In some cases, the Fire Department depends on a combination of its own investigations and information from the Tax Collector's Business Tax Division to identify businesses that must be inspected and permitted. Of all licensed businesses, vehicle parking lots are the most difficult to identify, because those businesses are the most unstable (that is, they are the most likely to change owners or go out of business).

Department of Public Health

The License Division collects a total of 35 license fees for the Department of Public Health, Bureau of Environmental Health and Bureau of Toxics. The purpose of these licenses is to protect the public's health, safety, and well-being, and to preserve and improve the quality of the environment. The DPH accomplishes this purpose through the delivery of programs and services that inspect, monitor and regulate the activities which it licenses. Categories of DPH licenses include Food Sanitation and Consumer Protection, Housing and Institutions, Recreational Health, Water Quality, Solid Waste, and Public Services. The Department of Public Health identifies businesses in need of licenses through its regular inspection and monitoring activities. Licenses issued by the DPH include laundry services, swimming pools and spas, food preparation services, dog kennels, and tattoo parlors.

Animal Care and Control

See Section II.2 of this report.

Rent Board

The Rent Board administers and enforces the Rent Ordinance, which provides for rent control and tenants' rights in the City. According to Section 37A.3 of the Administrative Code, the Rent Stabilization and Arbitration fee is established to require those who benefit from the Rent Board's administration of the Rent Ordinance to pay a fee. (This fee is directly related to the financial burden placed upon the City in carrying out the Rent Board's functions and duties. In other words, the amount of revenue collected from the Rent Stabilization and Arbitration fee is equal to the Rent Board's costs.) The License Division bills every San Francisco rental property for the Rent Stabilization and Arbitration fee, except for those that have filed a State Homeowner's Exemption with the Assessor's Office. Exemption from the Rent Stabilization and Arbitration fee, based on the Rent Ordinance, must be filed annually in response to the License Division bills.

PROBLEM STATEMENT

Given the Tax Collector's current organization structure, we found no major shortcomings in the administration of licenses. However, consolidating license billing with the property tax bill and the business registration fee billing would result in the following improvements: reduced duplication of effort; unified information systems; enhanced customer service; and increased collections. The following paragraphs detail these areas for improvement.

Greater Efficiency

Almost all of the individuals and businesses who receive bills from the License Division receive other bills from the Tax Collector's Office at other times of the year. For example, the License Division mails approximately 50,000[5] initial Rent Stabilization and Arbitration fee bills plus 56,500 notices of overdue bills,[6] at an estimated cost for mailing and printing alone of $31,000, not including staff time, materials and supplies, overhead, or other costs. All of these property owners also receive property tax bills. Combining the property tax bill with the Rent Stabilization and Arbitration fee billing would eliminate the 50,000 initial Rent Board billings, as well as many of the activities that accompany that mailing (such as opening envelopes or processing separate checks). (In regard to the collection of delinquent Rent Board fees, see below.) With the exception of certain Police Department licenses for individuals and dog licenses, all of the license billings are mailed to individuals or businesses who receive either a property tax bill or a business registration bill.

According to California codes, revenues collected for licenses should not exceed the cost to provide the license or service. For example, the amount charged for an Apartment House License should not exceed the City's cost for inspecting the apartment house and issuing the license. Therefore, an increase in license revenues or a decrease in costs should not result in any net gain to the General Fund or any other fund, unless the General Fund or another fund is supplementing the cost of issuing a license. (If license revenue exceeds the cost of issuing the license, then the license fee should either not be increased with inflation, until revenues equal costs, or the level of service associated with licensing should be increased.)

The following table indicates the total fee revenue and costs for five departments. The section of the table indicating the departments' costs to issue the license is based solely upon reports by the departments, and has not been confirmed independently by the Budget Analyst. In preparing the following table, we found that several departments, including the License Division of the Tax Collector's Office, use the revenues collected from issuing licenses in the prior year to estimate their expenditures to issue licenses in the upcoming year. In other words, the real cost to issue licenses has become separate from the amount of the license fee. However, an evaluation of the amount of the license fees was beyond the scope of this report.

The purpose of the table is to show the extent to which the cost to issue a license is not fully recovered by the departments, and, therefore, the extent to which the General Fund and other funds may benefit from reduced costs in issuing licenses. The Rent Board is non-General Fund supported, and the DPW is largely non-General Fund supported. The Police Department, the Fire Department, and the

[5] In June, 1994, San Francisco voters approved Proposition I which eliminates the Rent Stabilization and Arbitration fee exemption for owner-occupied properties with four units or less. The Tax Collector estimates that, as a result of Proposition I, 20,000 additional property owners will now be liable for the Rent Stabilization and Arbitration fee who were previously exempt.

[6] More notices of overdue bills are mailed than initial bills because overdue notices are required to be sent four times.

Department of Public Health are largely supported by the General Fund; any reduction in the cost of issuing licenses for these departments should therefore result in a direct benefit to the General Fund, up to the point where the cost of issuing the license is equal to the amount of revenue collected for that license.

The table below is divided into three sections which provide the following information: the first section shows the Tax Collector's costs for issuing the license, and the amount of revenue collected by the Tax Collector. The second section shows the user departments' cost for issuing the license, and the amount of revenue collected by the user departments. The third section shows the combined expenditures and revenues for both the Tax Collector and the user departments for issuing licenses. This table also shows the difference between expenditures and revenues; the amount of the difference is equal to the maximum benefit to the General Fund and other funds from increasing efficiency.[7]

Table 5
Net Cost for Issuing Licenses
Including User Department Inspection Costs and Tax Collector Administrative Costs, Less License Revenue
FY 1994-95

Section I: Tax Collector Administrative Costs and Revenue: FY 1994-95

	License Division	
	Revenue	Expenditure
Public Works	$3,207,115	$349,569
Police	744,800	162,446
Fire	421,260	41,716
Public Health	3,623,669	222,104
Rent Board	1,623,463	290,815*
TOTAL	$9,620,307	$1,066,650

*Includes costs for filing liens, at $143,000.

Section II: User Department Inspection Costs and Revenues: FY 1994-95

	License Division	
	Revenue	Expenditure
Public Works	$161,392	$1,866,747
Police	470,000	470,000
Fire	1,923,112	4,208,038
Public Health	541,777	8,780,713
Rent Board	*	1,332,648
TOTAL	$3,096,281	$16,658,146

* All license revenue for the Rent Board is collected by the Tax Collector's Office.

[7]Information regarding Animal Control and Care is not included in these tables. See Section II.2.

Table 5 (continued)

Section III: Net Cost for Issuing Licenses
Including User Department Inspection Costs and
Tax Collector Administrative Costs, Less License Revenue: FY 1994-95

	Revenue	Expenditure	Difference
Public Works	$3,368,507	$2,216,316	$1,152,191
Police	1,214,800	632,446	582,354
Fire	2,344,372	4,249,754	(1,905,382)
Public Health	4,165,446	9,002,817	(4,837,371)
Rent Board	1,623,463	1,623,463	0
Total, Net Expenditures	$12,716,311	$17,724,796	($5,008,208)

As the above table indicates, for DPW and Police Department licenses, the Tax Collector is collecting more than the reported cost of issuing the licenses, while, for the Fire Department and Department of Public Health licenses, the Tax Collector is collecting less than the reported cost of issuing the licenses. Since the Department of Public Health and the Fire Department are largely General Fund supported, the General Fund could benefit by a net amount of $5,008,208 by collecting as much as it costs to issue the licenses. This benefit could be gained in part by altering the amount of the fees (below, we recommend that the Board of Supervisors request a user fee study), and by decreasing the costs of issuing the licenses. This section of our report includes recommendations for improving the Tax Collector's efficiency and thus reducing the cost of issuing licenses.

As stated above, the costs in Table 2 are not based on the actual costs to collect license fees. However, costs to collect fees in general could be reduced by improving the Tax Collector's efficiency, as recommended in this section.

Unified Information

The License Division maintains a separate database from the Business Tax Division. Further, the Tax Collector's Office does not assign a single identification number for each taxpayer. As a result, the License Division might identify certain businesses that the Business Tax Division has not identified, and vice versa. One Division might also possess updated information that the other Division lacks, such as the closure of a business or a changed address. However, the two Divisions do not exchange adequate information. The only information exchange consists of monthly reports regarding parking lots and parking lot owners; information pertaining to any other type of business is not shared.

In some cases, parking garages may not be required to obtain a Business Registration Certificate, but all garages are required to obtain a fire permit. For example, a City-owned and operated garage would not be required to register with the Tax Collector's Office. Also, multiple garages operated by a single business would require only one Business Registration Certificate. However, the Business

Tax Division and the License Division were unable to provide accurate information to explain the discrepancy between the two listings. If the 200 unregistered garages must indeed register, the Business Tax Division is losing approximately $25,400 annually in registration fees (based on the actual average fee of $127), not including owing Gross Receipts and Payroll Taxes. In addition, to the extent that the Business Tax Division has identified parking lots of which the Fire Department is unaware, the Fire Department may be failing to license garages that must be inspected and permitted to protect the public welfare. Consolidating the License Division database with the Business Tax Division database would eliminate this miscommunication and inconsistency.

As stated above, additional revenue would be realized by the City, if the License Division has identified businesses that the Business Tax Division has not identified. For each business that the Business Tax Division does not register, the $25 to 500 annual business registration fee is forfeited. Gross receipts or payroll taxes may also be forfeited. Finally, the City's policies to enhance public health and safety would also be better served by consolidation. Unlicensed businesses would be identified and inspected by the user departments.

Enhanced Customer Service

Fragmentation compromises customer service because customers are unable to request information regarding all of their outstanding payments from a single source. Customers must be referred from one Division to another to receive complete information. Since the Divisions fail to communicate, information retained by the License Division may conflict with Business Tax Division information. The customer may have difficulty ascertaining the actual amount owed, even after discussing his or her outstanding accounts with several Divisions. For example, if one Division believes that a business is defunct, while another Division understands that the same business is still in operation, customers will have difficulty obtaining accurate information about that business's outstanding debts. (See Section I.3 of this report for more on Customer Service.)

In addition, taxpayers receive a series of bills, and must pay each bill separately. A single annual bill would facilitate a taxpayer's recordkeeping and bill paying.

Increased Collections

Under the existing system, collecting delinquent license revenues is difficult, for a number of reasons:

- √ License payments are small. It is therefore a low priority for the Tax Collector to collect individual delinquent license revenue;
- √ In regard to licenses and fees associated with property, filing liens is difficult and costly; and
- √ Taxpayers are often expected to remit several payments, for different amounts, to the Tax Collector's Office each year.

Since some licenses, fees and taxes are easier to collect than others (for example, almost all taxpayers pay their property tax bills), piggybacking harder-to-collect bills with easier-to-collect bills would increase collections of the harder-to-collect bills. To maximize this benefit, the Tax Collector would need to establish a mechanism to handle delinquent payments on consolidated bills (see below).

In FY 1993-94, outstanding DPW and Rent Board fees totalled $518,572, or 9.9 percent of the total billings for these fees, at $5,223,393. Based on a collection rate of 97.19 percent for secured property in FY 1993-94, the Tax Collector can expect the collections rate for most DPW and Rent Board fees to increase from the current 90.1 percent to the property tax collection rate of 97.19 percent.[8] For FY 1993-94, this would have amounted to additional revenue of $371,805 (based on projected collections of $5,076,626 at a 97.19 collections rate versus the $4,704,821 actually collected).

For FY 1994-95, outstanding Fire, Police, and Public Health fees totalled $589,629, or 12.67 percent of the total billings for these fees, at $4,651,991. Based on a current collection rate of approximately 72 percent for 1994 Business Registration fees, the Tax Collector can expect the City's business registration collection rate to improve. The Fire, Police, and Public Health fees currently have a collections rate of 87.33 percent. The actual amount of additional revenues that would be received from this improvement is difficult to estimate since not all businesses require Fire, Police or Public Health licenses.

IMPLEMENTATION

The following paragraphs provide specific recommendations for implementing the above improvements. The subsections, *Consolidation of Certain License Billings with Property Tax Billings, Consolidation of Certain License Billings with Business Registration Billings*, and *Administration of Licenses for Individuals*, provide detailed information for implementing the proposed reorganization, as well as specific estimates of the associated costs and benefits. The net benefit from these recommendations, including estimated cost reductions and increased revenues for all of the departments, would be $412,142 for the first year and $487,632 in following years.

[8]The collections rate for property tax might actually be marginally higher than 97.19 percent in the future, because the collections rate has been improving each year by at least .25 percent each year for the past three years.

Consolidation of Certain License Billings with Property Tax Billings

The Property Tax Division issues property tax bills twice a year. Most of the Department of Public Works licenses (Apartment House, Condominium, and Party Wall Structure, not Hotel) and the Rent Stabilization and Arbitration fee are associated with property, and could be consolidated with the property tax bill.

Administrative Reorganization

In order to consolidate specific license renewals with the Property Tax bill, administrative functions need to be reorganized. The License Division should transfer three positions to the Property Tax Division to complete the added workload associated with consolidating the bills. In addition, the database of license renewals will need to be combined with the Property Tax database and new tax forms must be created. This section of the report details the proposed changes to the Tax Collector's Office including the cost and savings associated with the consolidation of the aforementioned functions.

Current Costs for the License Division to Issue DPW & Rent Board Licenses		
Personnel, Including Salary and Benefits	Costs	
Department of Public Works (2.05 FTEs)	$349,569	
Rent Board (1.40 FTEs)	147,815	
Total Current Costs		$497,384
Proposed Costs for the Property Tax Division to Issue Licenses		
Personnel, Including Salaries and Benefits		
One full-time Principal Clerk (1408)	$51,467	
One full-time Account Clerk (1630)	40,524	
Total On-going Costs		$91,991
Proposed Additional First Year Costs		
One temporary Clerk (1404) (including salaries and benefits)	$37,740	
One-time computer programming	75,000	
Total Additional First Year Costs		112,740
Total First Year Costs		$204,731

The Property Tax Division would require one full-time Principal Clerk (1408), one full-time Account Clerk (1630) and one temporary Clerk (1404) to act as a customer service representative, at an estimated cost of $129,731 the first year and $91,991 in

subsequent years, including salaries and benefits. Therefore, the Tax Collector should transfer two individuals from the License Division to the Business Tax Division. (The customer service representative would be required for one year only, until taxpayers become accustomed to the new system and should be eliminated in ensuing years.) Consolidation would eliminate the cost to mail DPW and Rent Board renewal bills along with other non-personal services.

In addition, the Tax Collector should create a program that would consolidate the DPW, Rent Board and Property Tax bills. An outside vendor used by the Tax Collector for computer programming services estimates this one-time cost to be $75,000. Creation of the program would require approximately six months to one year.

Table 6

Costs and Savings to Consolidate DPW Licenses and Rent Board Fee with the Property Tax Bill

License Division's current annual costs to issue DPW and Rent Board Licenses	$497,384
First-year costs to consolidate billings	$204,731
On-going annual costs to consolidate billings	$91,991
First-year savings	$292,653
Annual savings	$405,393

Standardized Due Dates and Other Legislative Changes

In order to issue a consolidated property tax bill, the ordinances pertaining to DPW and Rent Board licenses would need to be standardized. Without this standardization, the consolidated bill would be infeasible, since each item on the consolidated bill would have separate due dates. To consolidate DPW and Rent Board fees with property tax bills, the Board of Supervisors would need to approve an amendment to the City's Administrative Code, so that DPW and Rent Board fees are due on the same day as the first property tax due date.

Additional legislative changes may be necessary to consolidate the billing. Such legislative changes should be identified by the City Attorney and proposed to the Board of Supervisors.

Standardized Collection Procedures

In order to consolidate the DPW and Rent Board fees with the Secured Property Tax bill, the Tax Collector would need to standardize collection procedures for all charges appearing on the consolidated property tax bill. Currently, the Tax Collector requires payment to be made in full based on the December 10 and April

10 billings for Secured Property Taxes: any partial payments are returned to the taxpayer (except in special circumstances). In contrast, the License Division accepts partial payments for license fees: only the unpaid balance is considered in calculating the debtor's delinquent accounts.

The Tax Collector has the authority to accept partial payments from the taxpayer for secured property taxes, with the approval of the Board of Supervisors.[9] However, we recommend no change to the Property Tax Division's current practice of refusing to accept partial payments, since accepting partial payments for secured property taxes would:

- √ cause additional work for the Property Tax Division in terms of mailing delinquent notices and processing multiple payments;
- √ create an incentive for taxpayers to mail partial payments instead of full payments; and
- √ require the establishment of a complicated payment priority system. For example, as stated above, many special assessments, such as unpaid, overdue water bills, are attached to the property tax bill in the form of liens. If partial payments were to be accepted, it would be unclear whether such payments should first cover the water liens (or other special assessments) or be put towards payment of the property tax.

In addition, the Property Tax Division returns only a small number of partial payments: of approximately 180,000 property tax payments, the Division returns 100 to 200 partial payments annually, or $^1/_{20}$ to $^1/_{10}$ of one percent.

In order to standardize collection procedures, the DPW and Rent Board fees should be classified as special assessments, since liens become automatic on property with delinquent special assessment payments. As soon as a Property Tax bill becomes delinquent, an automatic secured lien is placed on the property. This means that the property cannot be sold or refinanced until a Property Tax Division issues a Certificate of Redemption indicating that all debts on the property are cleared. There is no cost for these automatic secure liens on the Property Tax bill because such liens are administered internally by the Tax Collector. There is also no cost for the Property Tax Division to issue a Certificate of Redemption because it is a simple, computerized form. Thus, the current costs for filing liens for delinquent Rent Board fees will also be eliminated because the Rent Board fees will be consolidated as special assessments on the Property Tax bill.

Currently, the Tax Collector is required to mail two overdue notices to taxpayers before the bill becomes delinquent and liens are automatically filed, while the Rent Ordinance specifies that four reminder notices must be mailed to landlords delinquent in paying the Rent Stabilization and Arbitration fee. To standardize collection procedures, this Rent Board ordinance requirement should be eliminated, so that taxpayers would receive two notices for any and all property tax bill delinquencies.

---

[9]California Revenue and Taxation Code Section 2636.

Consolidation of Certain License Billings with Business Registration Billings

The Business Tax Division issues business registration bills once a year. All of the Fire Department and Department of Public Health licenses, the DPW Hotel license, and most Police Department licenses, are associated with businesses, and could be consolidated with the business registration bill. (The remaining Police Department licenses are issued to individuals. As an appendix to this report, we provide a complete list of Police Department licenses, sorted according to whether the license is collected from individuals or businesses. The Tax Collector should use this appendix to determine which licenses should be consolidated with the Business Registration bill, and which should be administered separately. In Section III.4 of this report, we discuss the categorization of Taxicab Licenses.)

Administrative Reorganization

In order to consolidate specific license renewals with the Business Registration bill, administrative functions need to be reorganized. The License Division should transfer three positions to the Business Tax Division to complete the added workload associated with consolidating the bills. In addition, the database of license renewals should be combined with the Business Tax database and new tax forms should be created. This section of this report details proposed changes to the Tax Collector's Office, including the costs and savings associated with the consolidation of the aforementioned functions.

Current Costs for the License Division to Issue Licenses

Personnel, Including Salary and Benefits		
Fire Department (.85 FTEs)	$41,716	
Police Department (1.85 FTEs)	162,446	
Department of Public Health (1.45 FTEs)	222,104	
Total Current Costs		$426,266

Resource Requirements for the Business Division to Issue Licenses

Personnel, Including Salary and Benefits		
One full-time Principal Account Clerk (1634)	$53,006	
One full-time Account Clerk (1630)	40,524	
Total Proposed On-going Costs		$93,530

Proposed Additional First Year Costs

One temporary Clerk (1404) (including salary and benefits)	$37,740	
One-time computer programming	75,000	
Total Additional First-Year Costs		112,740
Total Proposed First-Year Costs		$206,270

The Business Tax Division would require one full-time Principal Account Clerk (1634), one full-time Account Clerk (1630) and one temporary clerk (1404) to act as a customer service representative, at an estimated cost of $131,270 the first year and $93,530 in subsequent years, including salaries and benefits. Therefore, the Tax Collector should transfer three individuals from the License Division to the Business Tax Division. (The customer service representative would be required for one year only, until taxpayers become accustomed to the new system. The position should be eliminated in ensuing years.)

In addition, the Tax Collector should create a program that would consolidate the Police, Fire, DPH, and Business Tax bills. An outside vendor used by the Tax Collector for other computer programming services estimates this one-time cost to be $75,000. Creation of the program would require approximately six months to one year. Consolidation will eliminate the previous costs to mail Police, Fire, and DPW renewal bills.

Table 7

Costs and Savings to Consolidate Police, Fire & DPH Licenses with the Business Registration Bill

License Division's current annual costs to issue Police, Fire, and DPH Licenses	$426,266
First-year costs to consolidate billings	206,270
First-year savings	$219,996
On-going annual costs to consolidate billings	$93,530
Annual savings	$332,736

Standardized Due Dates and Other Legislative Changes

As with the property tax bill, all due dates for payables appearing on a consolidated business registration bill would need to be standardized. The Board of Supervisors would need to approve various amendments to the City's Administrative Code, so

that all businesses licenses would be due on the same day as the business registration due date.

Additional legislative changes may be necessary to consolidate the billing. Such legislative changes should be identified by the City Attorney and proposed to the Board of Supervisors.

Standardized Collection Procedures

Currently, the process for collecting delinquent business registration fees is to generate overdue notices and withhold Business Registration certificates. The process for collecting delinquent license revenue is to refer the delinquency back to the user department. The user department then takes appropriate enforcement action (i.e., revoking the permit). In most cases, the user department can either shut down a business operating without a permit, or begin the process of shutting down the business.

Since the Business Registration fee and license fees would be consolidated onto one bill, failure to pay the entire bill would result in both a delinquent Business Registration fee and License fee. The first step in collecting these delinquent fees should be the generation of one overdue notice to each delinquent taxpayer. If the taxpayer does not pay the bill or remits partial payment, he/she should receive neither his Business Registration Certificate nor his License Certificate. Quarterly, a list of taxpayers who are delinquent in their Business Registration and License fees should be forwarded to the appropriate user departments. Using this list, the user departments will be able to begin the process of shutting down a business that is operating without a license certificate. In an attempt to enforce payment, the taxpayer will be notified in his overdue notice of the potential consequences of operating without a license certificate. At the same time, the delinquent account should be forwarded to the Accounts Services Section of the Tax Collector's Office to begin collections procedures, (see Section I.1).

LICENSES FOR INDIVIDUALS

Licenses paid by individuals cannot be consolidated with other bills, because individuals do not necessarily owe business registration or property tax bills. Therefore, these licenses must be administered separately. However, since the number of such licenses is minimal, a separate License Division for these five or ten types of licenses is unnecessary. Since all of the individual licenses are related to the individuals' profession, the Business Tax Division should designate .5 FTE to administer licenses to individuals. (As noted in Section II.2 of this report, dog licenses should be issued as part of a dog licensing program under the Department of Animal Care and Control.) The cost of administering licenses to individuals under the Business Tax Division would be the same as the cost of administering those licenses under the License Division.

Reallocation of Responsibilities

The following paragraphs detail our recommended organizational, position and budgetary changes. The proposed reallocation of responsibilities in the Tax Collector's Office will result in the elimination of the License Division and a reduction in the number of staff required to implement licensing. These changes are indicated on the following charts. Chart 1 shows the current administration organization and function of the Tax Collector's Office. Chart 2 indicates the proposed administration organization and function beginning the second year after the reorganization. The first year, each Division would have one additional employee.

Chart 3
Current Tax Collector Organization and Function

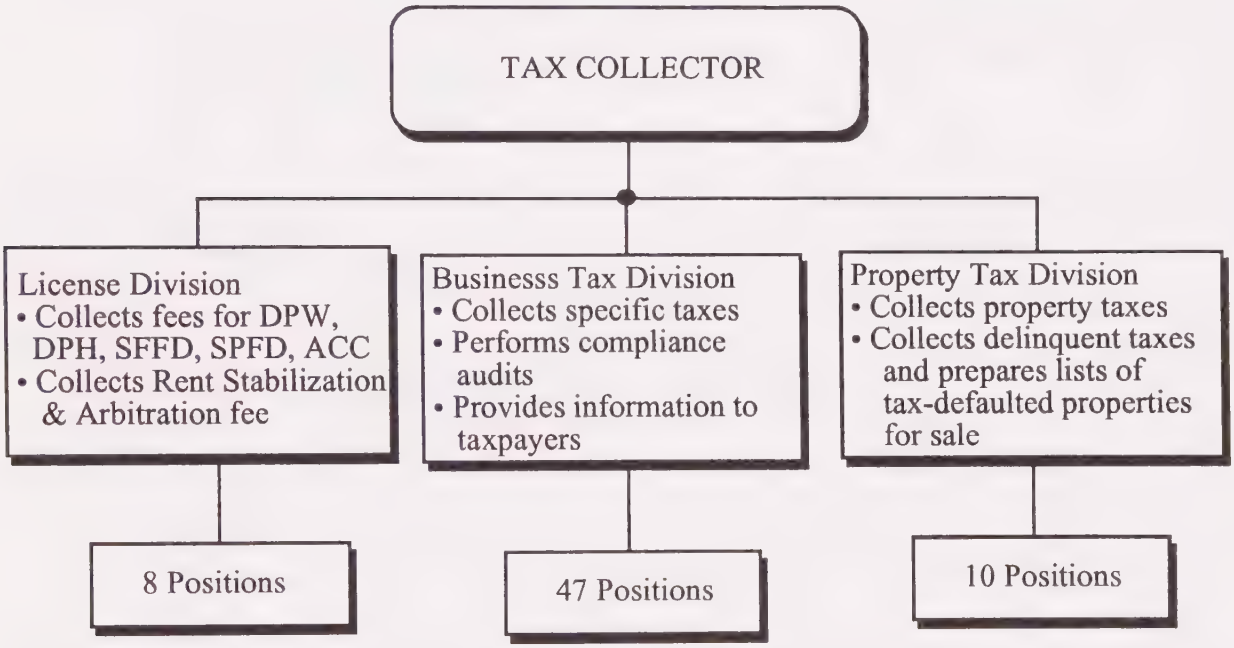
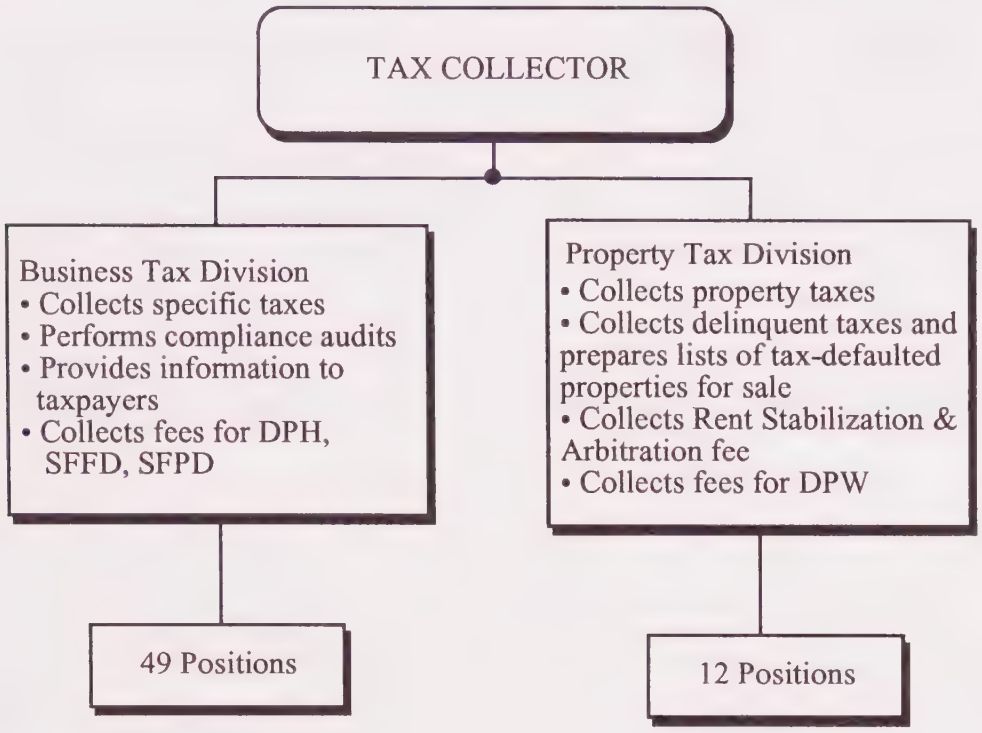


Chart 4
Proposed Tax Collector Organization and Function



Currently, eight positions in the License Division are included in the FY 1995-96 budget. Of these, six positions are General Fund positions and two are work order positions funded by the Rent Board. Staffing changes under the proposed reorganization include:

√ eliminating the 1410 Chief Clerk acting as the License Division Manager;

√ eliminating the two 1406 Senior Clerk positions;

√ modifying a 1404 Clerk to a one-year temporary position, and transferring that position to the Business Tax Division;

√ transferring one 1630 Account Clerk and one 1634 Principal Account Clerk to the Business Tax Division;

√ transferring one 1630 Account Clerk and one 1408 Principal Clerk to the Property Tax Division; and

√ adding one temporary position (a 1404 Clerk) for the Property Tax Division.

Specifically, the Board of Supervisors should amend the FY 1996-97 salary ordinance to reflect the following:

A reclassification of one permanent 1404 Clerk into a temporary position and a transfer of that position to the Property Tax Division:

FTE	Position Title	Salary and Benefits
1	1404 Clerk	$37,740

An increase of one temporary position:

FTE	Position Title	Salary and Benefits
1	1404 Clerk	$37,740
	Total Reductions less Total Increases (for the first year)	$102,650
	Total Reductions less Total Increases (for each additional year)	$178,130

An amendment to the Annual Salary Ordinance to eliminate three existing positions is a policy decision, based on whether (1) the Tax Collector's justification for the use of these positions in other Divisions; and (2) the Board of Supervisors prefers that such reductions be accomplished through attrition. These three positions are:

FTE	Position Title	Salary and Benefits
1	1410 Chief Clerk	$61,242
2	1406 Senior Clerk	79,148
	Total Reductions	$140,390

In FY 1997-98, the budget should be amended to eliminate two 1404 Clerks, at a cost of $75,480.

The Tax Collector's FY 1996-97 budget should be reduced by a total of $309,492 to reflect the elimination of the License Division, as follows:

- Object 130 Material and Supplies, by $30,826;
- Object 190 Other Non-Personal, by $180,510;
- Object 318 Building Repair, by $2,502;
- Object 340 Controller-DAT, by $44,933;

- Object 350 Reproduction, by $958; and
- Object 352 City Mail Service, by $49,763.

These reductions represent approximately 80 percent of the current expenditures by the License Division. The remaining 20 percent should be transferred to the Business Tax Division to support expenditures that will not be consolidated onto another tax bill, that is, licenses for individuals (particularly Taxicab Driver Licenses).

Finally, the Tax Collector's budget should be increased to reflect a one-time $150,000 cost for reprogramming the computer to handle consolidated bills.

In summary, first year costs would be reduced by a net of $262,142 (including reductions of $102,650 for salaries and fringe benefits and $309,492 for miscellaneous other costs, offset by a first year cost of $150,000). On-going costs would be reduced by $487,622 (including $178,130 for salaries and fringe benefits and $309,492 for other costs.)

SUMMARY

The License Division prepares and mails a separate bill for each license, even if an individual or business owes more than one license fee. Also, the property tax bill and the business registration bill are prepared and mailed separately from licenses, so that most individuals and businesses receive more than one bill from the Tax Collector each year. The Tax Collector should issue a consolidated property tax bill, including property taxes, the Rent Stabilization and Arbitration fee, and all four DPW fees. The Tax Collector should also issue a consolidated business registration bill, including the business registration fee, all Fire Department and DPH fees, and most Police Department fees. The Business Tax Division should allocate resources to administering license fees for individuals.

RECOMMENDATIONS

The City Attorney should:

1. Identify all legislative changes necessary to issue a consolidated property and business tax bill;

Board of Supervisors should:

2. Amend the FY 1996-97 Salary Standardization Ordinance as detailed in this report:

- Transfer four positions from the License Division to the Business Tax and Property Tax Divisions; and
- Establish one new temporary position.

An amendment to the Annual Salary Ordinance to eliminate three existing positions is a policy decision, based on whether (1) the Tax Collector's justification for the use of these positions in other Divisions; and (2) the Board of Supervisors prefers that such reductions be accomplished through attrition.

3. Amend the FY 1997-98 Salary Standardization Ordinance to reflect the reduction of the two temporary positions after one year as detailed in this report.

4. Amend the FY 1996-97 budget, in conformance with the recommendations contained in this report;

5. Amend the Administrative Code to standardize due dates for the consolidated bills, in conformance with the recommendations contained in this report;

6. Approve any other necessary legislative changes recommended by the City Attorney;

7. Amend the Rent Ordinance to eliminate the requirement that the Tax Collector mail four reminder notices to taxpayers delinquent in their Rent Board fee as detailed in this report.

The Tax Collector should:

8. Transfer one 1404 Clerk, one 1630 Account Clerk, and one 1408 Principal Clerk from the License Division to the Property Tax Division and one 1630 Account Clerk and one 1634 Principal Account Clerk from the License Division to the Business Tax Division;

9. Add one 1404 Temporary Clerk to the Business Tax Division;

10. Eliminate the License Division;

11. Direct the Controller's ISD or an outside vendor to create a combined billing system for a consolidated business registration and property tax bill; and

12. Implement consolidated billing, in accordance with the recommendations contained in this report.

COSTS AND BENEFITS

The proposed reallocation of licensing responsibilities will result in improved customer service, increased efficiencies and reduced administrative costs. Implementation of these proposed recommendations would result in one-time costs for Controller's ISD programming or an outside vendor's programming of

approximately $150,000 on-going reductions in total costs of $487,622. Also, the Tax Collector can expect the collections rate for license fees to increase from, 90.1 percent to 97.19 percent for DPW and for the Rent Board. In addition, the City's business registration collection rate should improve. Such increased collections would have resulted in additional revenues of at least $371,805 in FY 1993-94. Combined savings and increased revenues would therefore equal $859,427 at current salary and license fee revenues.

SECTION II.2: DOG LICENSES

Neither the Department of Animal Care and Control nor the Tax Collector conduct an Animal Licensing Program that would identify pet owners and require them to license their animals. As a result, only 6.8 percent (12,000 licensed dogs of a total estimated dog population of 177,000) of the City's dog population is licensed.

San Francisco charges a license fee of $6 for altered dogs and $12 for unaltered dogs, while other Bay Area jurisdictions charge up to $11 and $25, respectively.

If the Department of Animal Care and Control assumed responsibility for administering an Animal Licensing Program, and licensing fees were increased commensurate with Bay Area jurisdictions, the City could license an estimated 50,000 dogs, and realize a net increase in dog license revenues of $294,145.[1]

As part of our review of the License Division (see Section II.1 of this report), we considered the administration of dog licenses. The purpose of this review was to determine whether the existing organization structure maximizes dog license revenue.

Our review included identification of the dog license-related activities of the License Division of the Tax Collector's Office and the Department of Animal Care and Control (ACC), a comparison of San Francisco's dog licensing program with the programs of other jurisdictions, and a review of State and local codes to determine the potential uses of dog license revenue. We found that the number of dog licenses could be increased substantially, resulting in increased revenues as well as better care and control of San Francisco dogs, if the dog license program were administered by the Department of Animal Care and Control. We also found that the San Francisco dog license fee should be increased commensurate with fees in Bay Area jurisdictions.

This section of our report summarizes the activities of the Tax Collector and the Department of Animal Care and Control in regard to dog licenses, summarizes the

[1]Based on a weighted average cost per license for altered and altered dogs; subtracts increased costs to administer new licenses (see page 87).

practices of two other jurisdictions, and establishes specific recommendations for implementing this reorganization of activities.

BACKGROUND

The License Division of the Tax Collector's Office bills individuals for dog license renewals and issues dog tags. Under California law, counties must issue dog licenses. The amount of annual dog license fees is as follows:

Unaltered dogs	$12
Altered dogs	$6
Senior Citizen	$2
Replacement Tag	$1
Late Charge	$5

The Department of Animal Care and Control currently has no dedicated personnel to administer a dog license program. The Department performs no outreach activities to maintain or increase the number of dog licenses. Instead, counter personnel issue licenses or mail license applications based on customer-initiated contacts. ACC provides the names and addresses of licensed dog owners to the License Division of the Tax Collector's Office, and the License Division mails annual renewal billings to those individuals and processes payments.

The License Division mailed 7,154 dog license renewals in FY 1993-94. The Department of Animal Care and Control issues approximately 1,000 first time licenses a year directly, mostly for animals sold from the ACC shelter. ACC estimates that there are 177,000 dogs in the City, [2] of which approximately 12,000 are licensed dogs. Therefore, based on an approximate number of 12,000 licensed dogs, only 6.8 percent of the total dog population is licensed.[3]

[2] This estimate is based on national statistics prepared by the Society for the Prevention of Cruelty to Animals (SPCA) indicating that 37 percent of households have dogs, and each of these households has 1.5 dogs on average. San Francisco had 319,000 households in CY 1992. However, San Francisco's dog population may be lower than the national average, due to the high proportion of rental property.

[3] Since FY 1993-94, dog licenses can be issued for several months or up to 3 years as long as the license does not exceed the duration of the rabies shot. The Tax Collector's Licensing Division does not retain records indicating the number of licensed dogs in the City.

Both the Tax Collector and ACC collect dog license revenue. In FY 1993-94, the License Division collected the following dog license revenues:

Tax Collector
Dog License Revenue
FY 1993-94

Regular Fees	$71,287
Penalties	152
Total	$71,439[4]

In FY 1993-94, the Department of Animal Care and Control collected the following dog license revenues:

Department of Animal Care and Control
Dog License Revenue
FY 1993-94

Regular Fees	$23,814
Penalties	3,250
Total	$27,064

In total, the License Division and the Department of Animal Care and Control collected $98,503 in dog license revenues for FY 1993-94.

The Tax Collector's Office License Division has apportioned $47,145 to administer dog license fees in FY 1994-95. This amount is not based on anticipated expenditures; rather, it is based on a ratio of dog licenses to other licenses. This ratio was established several years ago and no longer reflects the correct apportionment of licenses. (For more information on the License Division's formula for apportioning expenditures, see Section II.1: Licensing.)

DOG LICENSE ADMINISTRATION BY THE DEPARTMENT OF ANIMAL CARE AND CONTROL

Although we found no major shortcomings in the Tax Collector's administration of dog licenses, given the current organization, improvements would result from removing dog license administration from the Tax Collector's Office and placing it under the Department of Animal Care and Control. The Department of Animal Care and Control, with sufficient resources, would be able to implement an Animal Licensing Program that includes outreach and education.

---

[4] Pet Hospital and Dog Kennel licenses are Department of Public Health licenses. As such, these revenues are not included in these totals. However, the Department of Animal Care and Control inspects these establishments, and receives a portion of the license revenue to support their inspection activities.

This section includes an explanation for why we believe a dog license program would be better administered by the Department of Animal Care and Control instead of the Tax Collector's Office. Following these paragraphs is a detailed calculation of the projected revenue increases from this proposed reorganization, as well as a projected budget for the program.

Why Transfer Responsibility away from the Tax Collector?

The following paragraphs describe why the Department of Animal Care and Control would be better suited to implement a dog licensing program than the Tax Collector's Office.

Mission

The mission of the Department of Animal Care and Control is to enforce all State and local animal control and welfare laws as well as provide comprehensive animal care and control services to San Francisco residents. The mission of the Tax Collector's Office is to collect fees for regulatory departments that have identified individuals or businesses requiring permits from the City. Because: (1) State law requires counties to issue dog licenses; (2) approximately 93 percent of all dog owners have not licensed their dogs; and (3) control of dogs is facilitated by dog licensing; the ACC should implement an animal licensing program as part of its mission to enforce State laws and to control animals.

Incentives

ACC is funded by a combination of General Fund monies and the City's Animal Welfare Fund. All animal license revenue must be deposited to the City's Animal Welfare Fund, and expended solely for animal welfare. All of ACC's expenditures in excess of the amount in the Animal Welfare Fund are supported by the General Fund. One advantage of placing all licensing activities under the Department of Animal Care and Control would be increased incentive to maximize revenue, since dog license revenues are deposited to the Animal Welfare Fund, and monies in the Animal Welfare Fund supports only ACC activities. In contrast, the Tax Collector receives no direct benefit from increases in dog license fees.

In recent years, the Department of Animal Care and Control's budget has decreased, although its responsibilities have increased. The Department's annual budget and authorized number of FTEs each fiscal year over the last six years, since the Department was formed, are as follows:

Table 8
Department of Animal Care and Control Annual Budget
FY 1990-91 to FY 1994-95

	FTE	Total Budget
FY 1989-90	37.0	$1,608,334
FY 1990-91	36.0	1,781,536
FY 1991-92	39.0	1,937,296
FY 1992-93	38.0	1,921,555
FY 1993-94	34.0	1,766,051
FY 1994-95	36.0	1,885,279

As the above table indicates, the Department of Animal Care and Control's annual budget has decreased by $52,017 (2.7 percent) since FY 1991-92, including decreases each year except for the current year. Before FY 1991-92, the Department's budget increased each year. The number of authorized FTEs has decreased by three (7.7 percent) since FY 1991-92. The Department advises that it has assumed responsibility for two additional functions — enforcement of the Vicious Dangerous Animal ordinance, and dead animal pick-up — since FY 1992-93.

Increased responsibilities and decreased resources would strengthen the Department's incentive to maximize revenue, since additional dog license revenues would provide special fund revenue that must support ACC's activities.

Expertise

The Department of Animal Care and Control has better access to dog owners and more expertise with animals than the Tax Collector's Office. Contacting veterinarians or visiting shot clinics, tasks related to an animal licensing program, would be beyond the scope of the Tax Collector's defined activities.

We surveyed two animal licensing programs to ascertain the types of activities they use to identify dog owners and increase the number of dog licenses. In San Mateo County, the Animal Licensing Division (part of the Environmental Services Agency) administers 55,000 dog licenses and one to two thousand cat licenses; outreach activities include creating and distributing animal licensing information packets to veterinarians and individuals and attending and providing animal licensing information at spay/neuter clinics and shot clinics. South Bay Animal Licensing, a new program administering licenses for the cities of San Jose, Milpitas, and Santa Clara, works with veterinarians, companies providing low-cost vaccinations and pet stores to identify unlicensed animals, and attends shot clinics and spay/neuter clinics to provide licensing information.

Many jurisdictions, including San Mateo County, have ordinances requiring veterinarians to forward a copy of the rabies vaccination certificate to the dog licensing department. Such a requirement would identify dog owners and provide a means to inform those owners about the licensing requirement. Revenue increases could be used to enforce the licensing requirement by supporting additional Animal Control Officers, who could be dedicated to locating and educating unlicensed dog owners. This type of activity enforced by ACC would increase the number of licensed dogs in the City but would be beyond the defined duties of the Tax Collector's Office.

Revenue Increases and Costs

Establishing an Animal Licensing Program would have the benefit of increasing the number of animal licenses, and consequently the amount of licensing revenue. We surveyed two animal licensing programs to compare their animal licensing revenue with San Francisco's, with the following results:

- ***South Bay Animal Licensing*** is in the midst of its first full fiscal year. When the program began in December, 1993, the combined jurisdictions had:
  - √ A total of 10,000 to 12,000 licensed dogs;
  - √ Annual program costs of $55,000; and
  - √ Annual revenue, based on $10 per license for altered dogs, of $100,000 to $120,000.

  Currently, the program has:
  - √ 27,000 licensed dogs (an increase of approximately 145 percent);
  - √ Annual program costs of $70,000 (an increase of 27 percent); and
  - √ Estimated annual revenue of $270,000 (an increase of 145 percent).

- ***San Mateo County Animal Licensing Division***

  Currently, the program has:
  - √ 55,000 licensed dogs;
  - √ Annual revenue, based on $11 per license for altered dogs, of $605,000.

  As noted above, San Francisco only has approximately 12,000 licensed dogs and annual revenue for dog licenses of $98,506.

To maximize animal license revenue, the City should charge fees commensurate with other Bay Area jurisdictions. The following table compares San Francisco's fees with those of the two other programs we surveyed.

Table 9

San Francisco's Annual Dog License Fees in Comparison with Other Bay Area Jurisdictions

	Unaltered[a]	Altered
South Bay Animal Licensing[b]	$25	$10
Contra Costa County	22	11
Tri-Cities[c]	20	10
San Mateo County	21	11
City of San Leandro	14	7
Alameda County	12	6
San Francisco County	**12**	**6**
City of Oakland	10	5

[a]Jurisdictions charge more for unaltered dogs to encourage owners to alter their animals
[b]Represents the cities of San Jose, Milpitas, and Santa Clara
[c] Represents cities of Fremont, Newark, and Union City

As the above table indicates, San Francisco's dog license costs are the second lowest fees of the 11 jurisdictions in our survey (South Bay Animal Licensing and Tri-Cities each represent three jurisdictions, as noted above). The average of the survey jurisdictions, not including San Francisco, is $19 for unaltered dogs and $9 for altered dogs (to calculate this average, we weighted South Bay Animal Licensing and Tri-Cities times three, because each represents three jurisdictions).

In order to charge fees that would maximize revenue and be within the range indicated by our survey of other Bay Area jurisdictions, San Francisco should increase its annual license fees from $12 to $19 for unaltered dogs, and from $6 to $9 for altered dogs. Such an increase, assuming the number of licensed dogs remains the same, would result in an increase in annual revenues of approximately $52,700, from $98,500 to $151,200.[5]

We recommend that the Department of Animal Care and Control be allocated one full-time staff person for each 10,000 licenses, to be funded from increased dog license revenues, based on the current practices of the Tax Collector's Office and the programs we surveyed, as follows:

[5] Given a current average of $8 per license a year, and a projected average of $12.60 a year. Since the beginning of FY 1993-1994 dog owners have been allowed to buy licenses for up to three years at any time of the year, depending on the length of time remaining on their rabies vaccination. The cost of a partial year license is a fraction of the annual cost. These estimates are based on one year renewals.

Table 10

Current Staffing Levels for Animal Licensing Programs

	Number of Dog Licenses	Number of FTEs	Approximate Number of FTEs per 10,000 Dog Licenses
San Francisco Tax Collector	12,000	1.0	.83
South Bay Animal Licensing[a]	40,000	4.0	1.00
San Mateo Animal Licensing Division	54,000	3.8	.70

[a]South Bay Animal Licensing staffing level is based on an anticipated number of licenses for June, 1995, of 40,000.

South Bay Animal Licensing and the San Mateo Animal Licensing Division perform all activities related to dog licenses, including data entry, deposits, database maintenance, and clerical work, using PC LAN-based systems without scanning capabilities.

The Animal Licensing Program under the Department of Animal Care and Control should implement a similar program, using similar staffing levels (one FTE per 10,000 licenses). These positions would be funded by dog license revenues itself. (The Controller would need to certify whether increased dog license revenue in the first year would support this new program. ACC should be required to report to the Board of Supervisors on the program's success in licensing dogs and gaining revenue after the first year. This report should indicate whether or not the program's revenues are sufficient to support its new costs.)

To provide ACC with sufficient resources to implement an effective dog license program and enforce dog licensing regulations, we recommend the addition of one permanent Office Supervisor, one temporary Shelter Service Representative, and one temporary Deputy Animal Control Officer. The permanent position would be funded by a decrease in the Tax Collector's budget, as noted below. The temporary positions would be made permanent, pending proof by the Department of Animal Care and Control that the number of dog licenses has increased by at least 10,000 after one year, and 20,000 after two years, to support the new positions. In each year following the second year, the Department of Animal Care and Control could receive an additional authorized position for each 10,000 increase in the number of dog licenses. Pending further review, a maximum number of employees should be set, since economies of scale would likely be realized.

Including the additional positions, the Department of Animal Care and Control should receive a one-year budget increase to support the Animal Licensing Program as follows:

Table 11

Proposed First Year Budget for Animal Care and Control Dog Licensing Program

Personnel			
1 permanent 1435 Office Supervisor (including mandatory fringe benefits)	$38,863		
1 temporary 1434 Shelter Svc. Representative (including mandatory fringe benefits)	28,187		
1 temporary 3372 Deputy Animal Control Officer (including mandatory fringe benefits)	29,517		
Total Personnel		$96,567	
Equipment			
Personal Computer and Printer		3,000	
Materials and Supplies			
Mailing/Postage	13,000		
Dog Tags	4,000		
Advertising	5,000		
Travel	1,000		
Office Equipment	2,500		
Office Supplies	1,500		
Computer Forms/Receipts	1,000		
Total Materials and Supplies		28,000	
Total Proposed Budget			$127,567

Based on the Animal Licensing Program stabilizing at approximately 50,000 dog licenses at an average charge per license of $12.60, total dog license revenue would be $630,000,[6] as compared with current revenues of $98,500. Based on maximum estimated costs of $284,500 to implement the Program (based on five full-time staff members plus all other costs), net revenue from the program would be $345,500, an increase of $294,145 over current net revenue of $51,355.[7] (The Department of Animal Care and Control currently licenses dogs as they are being adopted; as such, ACC incurs no incremental costs solely for dog licensing.)

Since the Tax Collector will no longer perform the functions associated with administering dog licenses, the Tax Collector's budget should be reduced by $47,145.

[6]Based on the Board of Supervisors approving an increase in dog license fees from $6 to $9 for altered dogs and $11 to $19 for unaltered dogs, commensurate with Bay Area jurisdictions.

[7]The current net revenue is based on $98,500 in revenues collected by the Tax Collector's License Division and Animal Care and Control less $47,145, the cost that the License Division attributes to the collection of dog licenses.

This budget reduction includes $37,710 in Permanent Salaries and Mandatory Fringe Benefits, which is the cost of one FTE 1404 Account Clerk (unless the Tax Collector provides justification for another use of this position) as well as a $9,435 reduction in Materials and Supplies. The $47,145 reduction in the Tax Collector's budget should be used to fund part of the increase in the Animal Care and Control budget. Thus, the net increase in funds to administer the dog licensing program will be $52,855 for FY 1995-96, to be supported by increased dog license fees.

SUMMARY

Currently, the Tax Collector's License Division estimates that there are 12,000 licensed dogs. Based on a total of 177,000 San Francisco dogs, only 6.9 percent of the City's dog population is licensed. Neither the Department of Animal Care and Control nor the Tax Collector conduct an Animal Licensing Program that would identify pet owners and require them to license their animals.

San Francisco charges a license fee of $12 for unaltered dogs and $6 for altered dogs, while Bay Area jurisdictions charge an average of $19 and $9, respectively.

RECOMMENDATIONS

The Board of Supervisors should:

1. Amend the Annual Salary Ordinance to:

- √ Reduce the number of authorized FTEs in the License Division of the Tax Collector's Office from 12 to 11, unless the Tax Collector provides justification to retain this position in another Division. Whether the position reduction should be done through attrition is a policy matter;
- √ Increase the number of authorized permanent 3373 Deputy Animal Control Officers in the Department of Animal Care and Control from 1 to 2; and
- √ Increase the number of temporary 3372 Animal Control Officers in the Department of Animal Care and Control from 0 to 1 for a total of 11 Animal Control Officers, granting that position permanent status after one year if the Department shows that the number of dog licenses has increased by 10,000.

2. Amend the FY 1995-96 budget to:

- √ Reduce the Tax Collector's budget by $48,441 including $37,710 in Permanent Salaries and Mandatory Fringe Benefits and $10,731 in Materials and Supplies ;
- √ Increase the Department of Animal Care and Control's budget by $100,000, to be funded by the Tax Collector's reduced costs plus increased dog license fees (to the extent certified by the Controller), in conformance with the recommendations contained in this report.

3. Approve an ordinance requiring veterinarians to provide lists of the names and addresses of pet owners to the Department of Animal Care and Control.

The Department of Animal Care and Control should:

4. Implement an Animal Licensing Program, in conformance with the recommendations contained in this report.

The Commission of Animal Control and Welfare should:

5. Approve an increase in fees for dog licenses to be commensurate with Bay Area jurisdictions, in accordance with the recommendations contained in this report.

COSTS/BENEFITS

Costs for administering the Animal Licensing Program would increase from approximately $47,145 to an estimated $127,567 in the first year and up to $284,500 after five years. Dog license revenues would increase from $98,500 to $630,000. Net revenue is currently $51,355; under the proposed new program, net revenue would be $345,500, an increase of $294,145.

SECTION III.1: BUSINESS TAX AUDITING

Auditors identify audit deficiencies for businesses that have not filed tax returns and/or have not registered with the City, when such unregistered/delinquent accounts should be pursued by a Collections Division. This practice cost the City $186,235 to $1,381,573 in uncollected revenue in FY 1993-94.

Audit productivity has declined substantially in the past three years, due to: (1) reduced accounting staff; (2) implementation of several legislative changes; (3) early retirements and long vacancies; and (4) coincidental implementation of the complex Business Tax System. Relieving auditors of taxpayer assistance ($470,924) and account maintenance ($1,177,311) duties would increase collected revenues from audited deficiencies by an estimated total of $1.6 million per year. The Business Tax Division has begun to implement this redirection of auditors to focus them on audit activities, and the decline began to reverse itself in FY 1993-94. Careful planning and budgeting for implementation of changes in tax regulations by the Tax Collector and the Board of Supervisors, and implementation of our recommendations for automation training and communications would also increase audit productivity. Development and enforcement of productivity standards to achieve an average of one audit completed weekly by each auditor would further increase collected revenues by an estimated $1 million. Total potential revenue increases of an estimated $2.8 to $4 million annually are identified in this section.

Selection of which firms the Tax Collector audits has been carried out on an ad hoc basis, without careful prioritization. While the Business Tax Division is in the process of implementing an automated selection system, the Division needs to study historical data to refine selection criteria. The Business Tax Division should also improve internal controls in the areas of audit assignments and account servicing.

A major function of the Business Tax Division of the Tax Collector's Office is to audit selected business tax accounts. Tax auditing can serve two broad purposes: (1) to obtain tax revenue that would otherwise have been lost; and (2) to improve voluntary taxpayer compliance. Audits of business taxpayer accounts in San Francisco have proved to be an important, though currently under-utilized, source of revenue. The additional value of audits as a deterrent to tax evasion cannot easily be measured, but is almost certainly significant.

This section focuses on the auditing unit of the Business Tax Division. However, issues related to the accounting, data entry and taxpayer services functions of the Division will also be discussed, because many problems of the auditing unit can be traced to diversion of auditor staff time and energy to these other functions. After examining the potential for increased auditor productivity, this section will propose improvements to the audit selection process and internal controls related to audits.

This section of our report does the following:

- reviews the trend in audit productivity, as measured by audited deficiency billings and collection of such billings;
- evaluates the Business Tax Division's practice of "auditing" delinquent and unregistered businesses;
- details non-audit duties of Business Tax Division auditors, including taxpayer assistance and account maintenance activities, as well as other factors that reduce audit productivity, including Business Tax System training/access problems and changes in tax regulations;
- proposes audit productivity standards;
- estimates the potential increase in auditing activity if auditors are relieved of certain non-audit duties and evaluated annually based on realistic productivity standards;
- describes the current audit selection practices and recommends a more systematic approach to audit selection; and
- recommends changes in the assignment of audits and servicing of audited accounts, to improve internal controls and insure equal treatment of all business taxpayers.

Section III.2, "Review of City Park Audit," follows this overview of business tax auditing in the Tax Collector's Office, and provides a detailed appraisal of one major audit conducted during FY 1993-94 by the Business Tax Division. That Section concludes with specific recommendations for improvements to audit policies and procedures, as well as better supervision of auditors.

BACKGROUND

Reductions in staffing that occurred in the Business Tax Division between FY1991-92 and FY 1993-94 coincided with the installation of the complex new automated Business Tax System (BTS). As the accounting staff declined from eleven in FY1991-92 to eight in FY1993-94, auditors increasingly had to fill the gap. In addition, the Business Tax Division has had to implement many changes to tax regulations in response to new legislation. These factors, along with several early retirements and prolonged vacancies, have resulted in a major decline in productivity and loss of focus within the Business Tax Division's Audit Unit. The auditing function has been hit hard by these problems, as evidenced by trends in the number of audits completed and total deficiency billings.

During the five years from FY1986-87 through FY1990-91, the auditing unit completed an average of 1,057 audits per year. In the following three years, during FY1991-92 through FY1993-94, however, the unit completed only an average of 320 audits per year, a nearly 70 percent decline. Over the past three years, the average auditor has completed less than one audit per week. Total audit deficiency billings did not decline as precipitously, because average billings per audit increased at the same time that fewer audits were conducted. Still, audit deficiency billings declined by 32 percent, from an inflation-adjusted annual average of $11,472,556 during FY1987-87 through FY1990-91, to an inflation adjusted annual average of $7,769,002 during FY1991-92 through FY1993-94. Actual collection of audit deficiency billings is carried out by the auditors, the Investigations Division and the Legal Division. The collection rate on audit deficiency billings has not declined as a percentage of annual billings. During the earlier five year period (FY1986-87 through FY1990-91), collections averaged 67.6 percent of audit deficiency billings, while in the past three fiscal years collections have averaged 69.2 percent of billings. The inflation adjusted annual average dollar collections from audit deficiency billings was $7,612,588 during FY1987-88 through FY 1990-91. The dollar value of audit deficiency collections declined by 28 percent in the following three years, to an inflation adjusted annual average of $5,496,548 during FY1991-92 through FY1993-94, reflecting the decline in billings.

During FY 1993-94, the Audit Unit started to improve audit productivity compared to the previous two years, as measured by number of audits completed (386), deficiency billings ($8.6 million) and collected revenues ($6.8 million).

These trends are illustrated in the following bar charts.

Chart 5

Audits Completed - FY 1986-87 through FY 1993-94

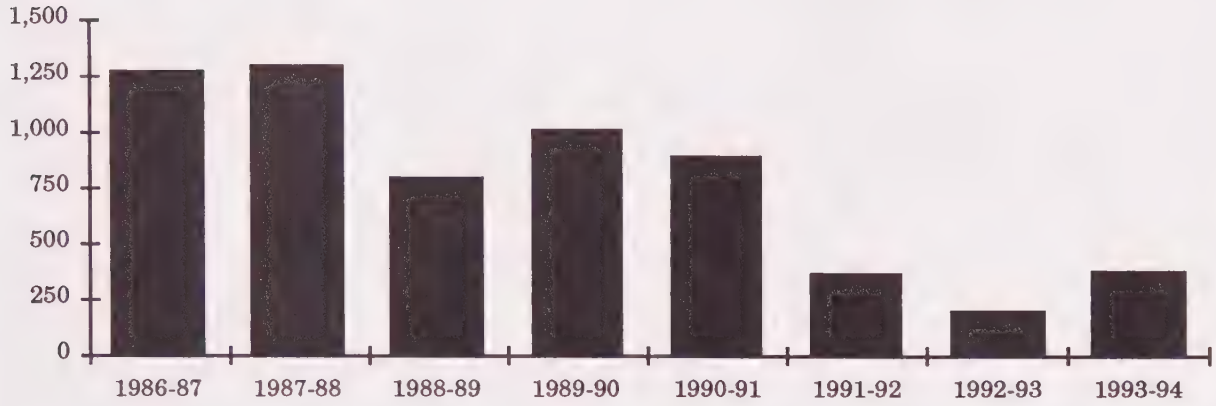
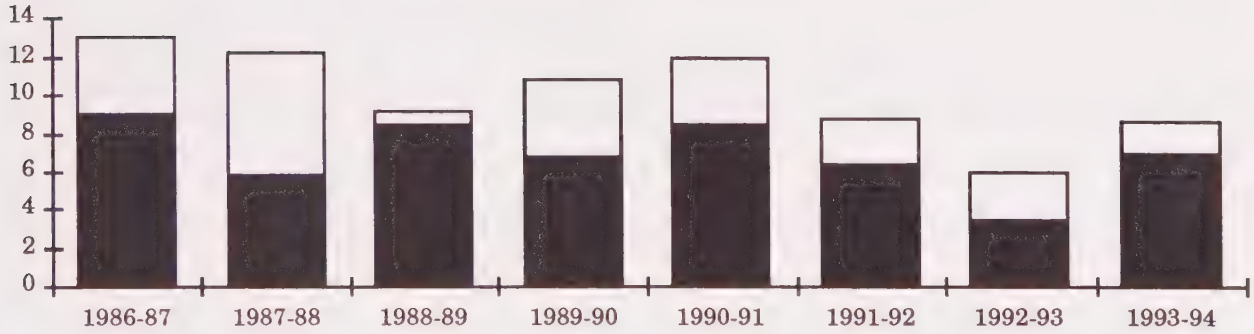


Chart 6

Audit Deficiency Billings and Collections
FY 1986-87 through FY 1993-94
(millions of dollars)



Note: Shaded area of bars shows collections; full bar shows billings. Audit deficiency billings and collections are in constant 1994 dollars.

BILLINGS FOR DELINQUENT AND UNREGISTERED BUSINESSES

The Business Tax Division has developed procedures to prevent a dramatic loss of revenues as a result of the reduction in the number of audits completed, as follows:

(1) Three auditors have been assigned part time to identifying and auditing "escapee" accounts -- businesses that have failed to register with the City of San Francisco. Because such businesses have never paid taxes to the City, auditing these businesses can produce significant new revenues. (A fuller discussion of new business identification is presented in Section III.3 of this management audit.)

(2) The audit unit makes large delinquent accounts — i.e., companies that have made significant tax payments in the past, but failed to pay in the most recent tax cycle — a primary target for audit. As one Principal Auditor stated, such audits guarantee "hard receivables" -- the auditor can be almost certain before starting the audit that it will produce a deficiency billing.

(3) The audit unit sends auditors to selected out-of-City and out-of-State locations, which has been highly productive in terms of deficiency billings and collections.

The first two types of audits noted above — audits of previously unregistered businesses or businesses that have not filed a return but paid taxes in the past — result in apparently high average per-audit billings, because the amount billed is equal to the total taxes owed by a business, rather than an incremental amount equal to the amount that the audit determines is owed, less the amount the business itself has already paid. For example, if a business calculates that it owes $50,000 in payroll taxes, and an audit determines that the business in fact owes $60,000, the audit billing would be equal to $10,000. In contrast, if a business has not filed, and the audit unit determines that the business owes $60,000, the audit billing would be equal to $60,000.

Although we support the Business Tax Division's efforts to sustain revenues despite decreasing resources, the first two functions are not auditing functions. Rather, these are collection functions. Under current policy, the Tax Collector's Investigations Division makes only very limited efforts to pursue delinquent business tax accounts (see Section IV.2). Under these circumstances, the current Business Tax Division practice of auditing delinquent and unregistered business accounts is reasonable. However, in our professional opinion, it is a waste of auditing resources to audit such delinquent accounts. These accounts should be referred for collection instead.

In Section IV.2 of this report, we recommend that the Tax Collector establish a consolidated Collections Division, which would automatically perform certain non-resource intensive collections activities. Accounts for businesses that are out of compliance with City ordinances requiring them to register and file tax returns should be forwarded to this Collections Division. Such businesses would then receive at least two notices that their taxes and registration fees are overdue; failure to respond would result in the seizure of the businesses' financial assets, and subsequent further action, if necessary and appropriate. The Tax Collector has already established methods for calculating amounts owed by businesses that have not registered and/or filed tax returns (see Section IV.1 of this report). The Collections Division would collect the amount owed based on these estimators.

An audit should only be performed on delinquent accounts prior to the Tax Collector taking legal action on these accounts. The audit should be the last step in the collection process. Such accounts should not be audited unless all of the regular (less labor intensive) collection activities fail to produce a statement and payment.[1]

The Business Tax Division was unable to provide any information regarding what portion of the 386 "audits" performed in 1993-94 were actually delinquent and unregistered business calculations, as opposed to regular audits of businesses for compliance with the Municipal Code registration and tax return filing requirements. Because such information was not available, we were unable to determine the actual average revenue from regular audits versus pursuit of delinquent revenue.

To estimate the amount of revenue that could have been collected by pursuing delinquent accounts through letters and liens in addition to performing 386 regular audits, we assumed that the average audit deficiency for regular audits is $13,318.[2] We were unable to estimate the average delinquent and/or unregistered

[1]This recommendation is not meant to preclude the selection of such accounts for audit based on other criteria, as discussed later in this section.

[2]$13,318 is the average per-audit deficiency in FY 1990-91, adjusted for inflation. In the following paragraphs of this section of our report, we recommend efficiency improvements that will result in 928 total recommended annual audits. We selected FY 1990-91 because the number of audits performed that year — 898 — was the closest to the number of audits we recommend that the Tax Collector perform annually. $13,318 probably understates the average audit deficiency that could be identified if only 386 audits are performed, because, on average, each additional audit likely results in lower revenue. Therefore, our FY 1993-94 estimates are conservative.

account without any supporting data; we therefore established a range of $26,755 to $40,722.[3]

Total combined collections would have been higher because the Collections Division would have brought in approximately the same revenue from delinquent and unregistered accounts as did the Audit Unit (using practices recommended in Section IV.2 of this report), while the Audit Unit would still have been able to audit a total of 386 regular audits, therefore reaching more businesses altogether.

Assuming that two-thirds (259) of the total 386 FY 1993-94 audits were delinquent and/or unregistered business accounts, the Tax Collector would have collected total revenue of $8,207,799, including $5,140,748 for 386 regular audits, plus $6,929,545 (259 delinquent accounts times $26,755 per account), discounted 68 percent to equal the Tax Collector's collection rates for audit deficiencies. This represents an increase of $1,381,573 over the $6,826,226 actually collected.

Assuming the reverse — that one-third (127) of the total 386 FY 1993-94 audits was delinquent and/or unregistered business accounts — the Tax Collector would have collected total revenue of $7,012,461, including $5,140,748 for 386 regular audits, plus $5,171,694 (127 delinquent accounts times $40,722 per account), discounted 68 percent to equal the Tax Collector's collection rates for audit deficiencies. This represents an increase of $186,235 over the $6,826,226 actually collected.

---

[3]The low end of this range represents the average delinquent and/or registered account if one-third of the "audits" (127) was regular audits, and two-thirds (259) were delinquent revenue billings, as follows:

127 regular audits x $13,318 each = $1,691,386

Total amount of audit billings for FY 1993-94 = $8,621,045

$8,621,045 (total amount of billings) - $1,691,386 (amt. identified through regular audits) = $6,929,659 (total amount identified for delinquent/unregistered businesses)

$6,929,659 ÷ 259 delinquent/unregistered = $26,755 average billing per delinquent/unregistered

The high end assumes the reverse: that two-thirds of the "audits" were regular audits and one-third was delinquent revenue billings, as follows:

259 regular audits x $13,318 each = $3,449,362

Total amount of audit billings for FY 1993-94 = $8,621,045

$8,621,045 (total amount of billings) - $3,449,362 (amt. identified through regular audits) = $5,171,683 (total amount identified for delinquent/unregistered businesses)

$9,929,659 ÷ 127 delinquent/unregistered = $40,722 average billing per delinquent/unregistered

The following table indicates these estimated increased revenues from referring delinquent accounts to a Collections Division instead of using auditing resources to identify these revenues.

Table 12

Two Estimates for Increased Revenue from Referring Delinquent and Unregistered Businesses to a Collections Division
FY 1993-94

Number of Regular Audits	Number of Delinquent/ Unregistered	Revenue from Audits	Revenue from Collections	Collections Rate	Total Revenue	Increase Over Actual 1993-94 Collections of $6,826,226
386	259	$5,140,748	$6,929,545	68%	$8,207,799	$1,381,573
386	127	5,140,748	5,171,694	68%	7,012,461	186,235

AUDIT SELECTION

Under the practice in place during the conduct of this audit, three Principal Auditors were each assigned audit responsibilities for all firms whose business names start with a particular portion of the alphabet. The Principal Auditors periodically received printouts of the full list of such firms, along with information about their tax payments over the past two to three years. They applied informal rules of thumb to select audit candidates from these printouts manually. The Principal Auditors were not required to use one agreed upon set of selection criteria, and do not have to obtain approval or explain their selection rationale to the Chief Auditor.

The selection of business taxpayers for audit should be made on the basis of conscious policy, and should take full advantage of the database that is available to the Tax Collector. Tax auditing can serve two broad purposes: (1) to obtain revenue that would otherwise have been lost; and (2) to improve voluntary taxpayer compliance. Audit selection furthers the goal of revenue maximization when the auditing agency identifies and sorts accounts on the basis of variables that indicate likely major tax discrepancies. Audit selection works to improve voluntary compliance when accounts are sorted to obtain an audit list that includes businesses from many different sectors of the local economy. In this way, the auditing program achieves wider notoriety, and taxpayers throughout the business community gradually become aware that there is a chance that they will be audited.

The Principal Auditors in the Tax Collector's Office use selection criteria that are designed to maximize revenues. There is no effort to use the audit function to promote voluntary taxpayer compliance. In interviews the Principal Auditors mentioned a variety of balance sheet indicators that the auditors use to determine

whether a tax statement might be inaccurate: e.g. a total salary figure that looks unrealistically low compared to the number of employees, an unusually high accounts receivable balance, or an unusual number of exemptions. The Business Tax Division prepared a lengthy list of such selection criteria during FY 1993-94 in an unsuccessful effort to computerize the selection process. The indicators were not prioritized, so that the program prepared by the Controller's ISD selected 6,000 accounts, rather than the 500 that the Chief Auditor felt could realistically be audited in a year. The selected accounts were not prioritized, and the program was useless to the Division. Although Business Tax Division staff suggested that this reflected a problem with the ISD, the prioritization of selection criteria is as important as the identification of the criteria, and should be developed by the tax experts, not the computer experts.

The Chief Auditor is currently implementing a revised selection process, under which 18 criteria are used to provide Principal Auditors with lists from which they can select accounts for audit. This approach is an improvement over past practice. It should be used as a starting point from which to develop a more sophisticated selection system that takes full advantage of the data available to the Tax Collector.

In summary, the selection of accounts for audit by Principal Auditors, acting independently of each other and the Chief Auditor, has several major disadvantages. The practice results in uncoordinated, possibly conflicting, policy decisions by staff. The incentive to boost audit deficiency billings to make an audit team look productive may not result in the best overall mix of audits. Finally, while the auditing staff has highly valuable experience that should contribute to the development of an audit selection process, the BTS system should provide data that could be used to test assumptions, and possibly identify valuable new selection criteria. Historical audit collection data, as well as audit selection methodology used by the IRS and other cities, should be systematically reviewed to verify and refine the rules of thumb that have been developed.

As a first step, the Tax Collector should determine what kind of balance he wishes to strike between the audit goals of revenue maximization and encouragement of voluntary business taxpayer compliance. This will establish the proportion of audits to be selected for their collection potential, and the proportion to be selected by business type to gain wider awareness of the audit program. In the opinion of the Budget Analyst, at least 15 percent of annual audits should be selected to achieve notoriety for the audit program, rather than exclusively for immediate revenue maximization purposes. Once that policy has been established, the Chief Auditor should refine the automated selection process to make full use of available information. The automated process should be designed to select a realistic number of audits, taking into account that a projected (and limited) number of escaped (previously unregistered) business audits, delinquent account audits and other special purpose audits will also be required during the year, chiefly to enable the Tax Collector to take legal action on these accounts.

AUDIT PRODUCTIVITY

Opportunities to increase revenues and taxpayer compliance through business audits are being lost because the amount of time devoted to auditing has declined so dramatically. The reduction of auditor time for audit activities resulted primarily because of: (1) auditor staffing of taxpayer services; (2) auditor responsibilities for Business Tax Division accounting and administrative functions; (3) ineffective user training and input into modification of the BTS system; (4) time-consuming auditor involvement in implementation of ongoing changes in business tax regulations; and (5) the failure of supervisors to enforce realistic productivity standards for the auditors.

Auditor Taxpayer Assistance Activities

The Tax Collector's Office does not have a centralized Taxpayer Assistance Unit, so the Business Tax Division is responsible for answering all telephone questions and in-person inquiries regarding matters related to business taxes. Auditing personnel staff the telephones and provide technical support to the clerical staff who handle in-person inquiries. All auditors (except the four Principal Auditors) spend one day per week in the business taxpayer services unit.

As detailed in Section I.3 on Taxpayer Assistance, during the period when this report was prepared the Tax Collector was in the planning and early implementation stages of an effort to reorganize taxpayer assistance. An experienced Principal Account Clerk has been assigned to supervise the clerical staff in the taxpayer services unit, starting in February, 1995. At the same time, auditors are no longer required to staff taxpayer assistance desks on a regular basis. Consideration is being given to forming a consolidated taxpayer assistance group with specialized personnel.

A new telephone system that includes options for taxpayers to access recorded information was implemented in 1995. Telephone inquiries from taxpayers who wish to speak to a staff person, however, are still being routed to Auditors. Because the system has a series of recorded messages providing basic information, the volume of calls to auditors is expected to decrease. The Chief Auditor expects to assign an average of two auditors each day, on a rotating basis, to answer telephones. During peak assistance periods, more auditors would be asked to answer telephones. Two auditors per day would represent a 50 percent decrease (from four FTEs) in auditor time devoted to taxpayer assistance. However, under current practices of routing all calls to auditors, we do not believe that such a reduction can be achieved without sharply reducing the number of telephone calls that are answered. The Tax Collector could make a policy decision to reduce telephone taxpayer assistance, but as detailed in Section I.3, an internal working group in the Tax Collector's Office has found that frequent busy signals and unstaffed telephones is already a source of many taxpayer complaints.

A large proportion of telephone inquiries could and should be routed to taxpayer assistance or accounting personnel, thereby enabling the Chief Auditor to actually achieve a 50 percent decrease in auditor telephone assistance time. The use of auditors to answer all telephone inquiries appears to be driven by a combination of inadequate staffing of taxpayer assistance, and by the restrictive computer access and system training practices that limit the effectiveness of accounting personnel in checking account status. The Chief Auditor should require auditors to log time spent on telephone taxpayer assistance, and the type of assistance required. The logs should indicate categories of telephone inquiries that could be handled by the taxpayer assistance group or by accounting personnel, and do not require an auditor's expertise. The telephone system could be adjusted to forward such calls to the taxpayer assistance group, except during periods when that group has no time due to the volume of in-person assistance requests.

As discussed in Section I.3 of this management audit, the Tax Collector's Office should eventually establish a consolidated Taxpayer Assistance Unit where taxpayers can obtain information on business taxes, property taxes and licenses in a single telephone call or in-person inquiry. Auditors should not be required to answer most in-person or telephone inquiries, because most taxpayer questions are related either to general requirements or to individual account information, either of which could be answered by accounting or clerical staff, if they are fully trained to use the BTS programs and have a basic knowledge of San Francisco's business tax procedures.

Auditor Account Maintenance Activities

The Statement Processing Unit of the Business Tax Division is responsible for inputting data from completed business registration and business tax statements to the BTS data base, reconciling payment records, updating accounts to reflect changes in address, business name, etc., and handling the research and posting of irregular business tax payments.

Implementation of the BTS automated tax system in December of 1991 increased the workload for the Statement Processing Unit. The BTS system accepts more detailed information than the old business tax database accepted. For example, the old system showed only the lump sum of tax payments for a business, even if that business had multiple locations within the City. The new BTS system shows taxes paid for each address or fictitious name under which a corporation does business. However, with these on-line capabilities comes the need to input a large volume of data from tax statements and registration forms.

As data entry requirements increased after installation of BTS, and accounting staff was reduced, auditors have been used to perform account update functions and to do check control (analysis and posting of irregular checks -- that is, cases where the cashier is unsure of the source or purpose of a payment). Starting in

FY1991-92, an entire team of 4 Auditors, a Senior Auditor and a Principal Auditor was relieved of all audit responsibilities in order to perform these account maintenance functions and other administrative tasks, such as coordinating taxpayer services staffing assignments and answering correspondence.

Six new positions were authorized for the Business Tax Division in the FY1994-95 budget. They are: a 1630 Account Clerk, a 1632 Senior Account Clerk, a 1654 Principal Accounts, a 1656 Head Accountant, an 1818 MIS Specialist II, and an 1822 Administrative Analyst. The Tax Collector stated in his budget request that these new positions would relieve the clerical functions now performed by auditors, thereby enabling auditors to collect an additional $3 million in annual revenues.[4] However, of the six authorized new positions, two were hired in early 1995, and the other four still had not been hired as of the writing of this report. The Chief Auditor stated that he planned to have auditors continue to perform account maintenance functions during a transition period, and to train the new accounting staff. The Tax Collector should make filling these accounting positions a high priority.[5] The Chief Auditor should, as planned, return the administrative audit team to full-time, regular audit duties as soon as the new accounting staff can be hired and trained to take over their administrative/account maintenance duties. The Chief Auditor reports that he plans to establish an Accounting and Statements Unit within the Business Tax Division when these hires have been completed, composed of accounting and statement entry staff. He further reports that he has started to assign audits to the audit team that has been devoted to administrative duties.

In Section I.1 of this report we recommend the establishment of a consolidated Accounting Division. Once such a division exists, the accounting and statement entry responsibilities currently handled by the Business Tax Division would be transferred, along with accounting/data entry staff, to the new Accounting Division.

Business Tax System (BTS) Inefficiencies

Even three years after BTS was installed, auditors and clerical staff state that labor-saving corrections have not been carried out. For example, in order to input a change of address the operator must adjust three screens -- one for the mailing address, one for the owner's address, and one for the business address -- even if the address is identical for all three. Although data entry and auditor staff have made written reports about such problems, many remain to be resolved.

---

[4]Auditors in the Business Tax Division will not generate additional revenue in FY1994-95, in part because of the lengthy hiring process for the new accounting staff, and in part because, as discussed in Section III.5, the Amnesty Program required a major investment of Auditor time during FY1994-95.

[5]While unnecessary delays in hiring should not be tolerated, the Chief Auditor should take care to insure that any new staff -- particularly accounting positions -- have the skills and experience to enable them to master the Tax Collector's automated systems.

In other cases, auditors waste time in using the BTS system because they are not aware of the best ways to obtain the information they need or input the data they must record. For example, some auditors are unaware of "hot keys" that would enable them to increase access speed to key screens on the system. Even Principal Auditors told us that they were more comfortable selecting audits from index card files than from the BTS files. The value of an automated system is only as good as the ability of its users to take advantage of the data management tools it provides.

Overly restrictive security measures also waste auditors' time. There has been a tendency to restrict clerical and lower level accounting staff from making even routine changes to accounts, ostensibly for internal control purposes. Auditors frequently have to make these changes. Auditors are also called upon by staff from other Divisions, such as the Clearance Unit of the Investigations Division, to look up the status of taxpayer accounts because Clearance Unit staff do not have full access to such information. This practice should be discontinued with the hiring of new supervisory level accounting staff in 1995. As long as proper supervision is provided, there is no reason to limit the ability of clerical and accounting staff to perform functions that fall appropriately within their jurisdiction.

Our recommendations for improving automation in the Tax Collector's Office are presented in Section I.2. Clearly, the staff of the Business Tax Division should have an effective channel for requesting and obtaining modifications to the BTS system based on their experience as users. Furthermore, all staff need system overview training and one-on-one training follow-up to enable them to make full use of the system and to ensure that they are aware of how the information that they input is used by other staff in the Tax Collector's Office.

Impact of Changes in Tax Regulations

When tax regulations are changed by the passage of new legislation, the Tax Collector's Office must educate the public and implement the reform. The following chart identifies local business tax ordinances approved during a three-year period from 1992 through 1995.

Chart 7

Local Business Tax Ordinances Approved from February, 1992 through February, 1995

Ordinance No.	Legislation Subject	Date Approved
9-95	Tax Collection Mechanism for Family Support	January, 1995
429-94	Small Business Tax Exemption	December, 1994
339-94	Business/Payroll Tax Amnesty	October, 1994
267-94	Changes to Firearms/Ammun Bz Tax	July, 1994
250-94	Stadium Operator Admission Tax Increase	July, 1994
236-94	Transfer Tax Exemption - Domestic. Partners	June, 1994
179-94	Reversion of Threshold & Graduated Tax Rates	May, 1994
195-94	New Firearms/Ammunition Business Tax	May, 1994
419-93	Emergency Response Fee	December, 1993
356-93	Registration Required for Fictitious Bz Name	November, 1993
310-93	Parking Tax Rate Changes	October, 1993
306-93	Vehicle Renter Tax Changes	September, 1993
273-93	Bz Threshold & Hotel & Parking Prepayments	August, 1993
244-93	Transient Occup. Tax Surcharge Increase	August, 1993
261-93	Increased Gross Receipts for Vehicle Renters	August, 1993
262-93	Utility Users Tax-Cellular Telephones	August, 1993
273-93	Graduated Payroll Expense Tax Rates	August, 1993
199-93	New Jobs Tax Credit	June, 1993
227-93	Transient Occup. Tax in Redevelopment Areas	June, 1993
166-93	Stadium Operator Admission Tax Change	May, 1993
200-93	Enterprise Zone Tax Credit	February, 1992

During this three year period between February, 1992 and February, 1995, a total of 21 new local ordinances were approved which directly effected the operations of the Tax Collector's Office. In fact, 17 of these local ordinances were approved during the 15-month period from May, 1993 through July, 1994.

Of the total 21 ordinances approved during this three year period, the Tax Collector reports that two of these ordinances were initiated by the Tax Collector's Office. The remaining 19 ordinances, or 90 percent were initiated by the Board of Supervisors or Mayor's Office. The Department is not always consulted prior to an ordinance change, and does not always provide the Board of Supervisors with a detailed, realistic estimate of the staff or resources required to implement the new program.

In almost all cases, the staff that is diverted to address new ordinance changes would otherwise be working on ongoing tax collection revenue activities. In some cases, the Tax Collector relies on Investigators to assist on new legislative activities which results in the delay in the collection of tax revenues and in the potential loss of a portion of those tax revenues, although the actual amount of such loss is not possible to quantify. However, it has been the common practice of

the Tax Collector's Office to routinely divert audit staff for new ordinance activities.

For example, the Business Tax Amnesty Program that was conducted in December, 1994 and January, 1995 essentially halted audit activity for at least a three-month period, as Auditors were needed to design forms, review applications, distribute information to office buildings, answer telephone inquiries and input data following the close of the application period.

The Board of Supervisors should request an analysis from the Tax Collector of any proposed tax ordinance, both in terms of the Tax Collector's assessment of the ordinance's impact on taxpayers and revenue collection, and in terms of the Tax Collector's estimate of required staffing. The proposed ordinance should include funding for adequate temporary staffing to prevent undue disruption of the ongoing activities of the Tax Collector's Office. Unfortunately, in some cases it may be impossible to hire temporary workers to perform work that would otherwise be assigned to Auditors, if specific technical knowledge of tax procedures is required. However, the Business Tax Division should strive to develop a stable list of temporary workers who can be trained in local tax laws and procedures. Thus Budget Analyst recognizes that Civil Service rules limiting the number of hours that a temporary employee can work for the City per year may impede such efforts to retain experienced temporary staff.

Productivity Standards

During FY1993-94, Auditors in the Business Tax Division in the three teams that were assigned to audit duty completed only an average of 26 audits per Auditor. (Nevertheless, this is a substantial increase over the 15 audits per Auditor that were completed during FY1992-93.) During the previous two years (FY1991-92 and FY1992-93), low productivity was understandable, not only because the BTS system was new, but also because the audit unit lost productive personnel to several vacancies. However, by FY1993-94 Auditors should have been reasonably comfortable with the BTS system, and a review of vacant positions shows that only .17 FTE in Auditor time was lost due to vacancies. Even with conflicting demands on Auditor's time, as detailed above, the Chief Auditor and Principal Auditors should have been able to obtain higher productivity from the audit staff.

In the five year period from FY1986-87 through FY1990-91, Auditors completed an average of 51 audits per year, per Auditor. This level of audit productivity was significantly effected in the following years by the disruption from implementation of the BTS, declines in accounting staff and ordinance changes that drew auditors into non-audit work. It is time for the Business Tax Division to develop and enforce productivity standards for Auditors to return them at least to pre-BTS efficiency levels. The Budget Analyst recognizes that the increased number of audits of previously unregistered businesses -- which might require multi-year reviews -- has increased the average amount of time required to

complete an audit.[6] We therefore recommend a productivity goal based on the general concept that an auditor should be able to complete at least one audit per week. After subtracting vacation, holiday and sick leave time, this would amount to approximately 46 audits per year per auditor.[7]

Realistic productivity goals must take into account the variations in audit complexity and length. Rather than simply establishing a minimum standard of 46 audits per year per auditor, the Chief Auditor will have to develop a system for weighting the productivity value of audits to reflect these variations. Prior to distribution of audit assignments, the Principal Auditors should agree on the value that will be assigned to each audit, so that workload can be balanced and accomplishments evaluated in terms of a 46 audit per year equivalent.

The Chief Auditor should implement a process of personnel evaluation that measures auditor productivity, and evaluates the performance of Principal Auditors in terms of their ability to obtain the desired level of productivity from their staff.[8]

Potential Increase in Auditing Activity

The Audit Unit could generate a major increase in audit deficiency billings if the changes proposed by the Division and recommended above by the Budget Analyst are made. We have projected potential revenues using realistic assumptions, without augmenting Auditor staffing.[9]

√ Reduce Auditor telephone taxpayer assistance duties by 50 percent, providing an additional 2 full time equivalent (FTEs) of Auditor time for audits. Assuming 52 additional audits per year (at 26 audits per auditor per year) with average deficiency billings of $13,318, additional deficiency billings of $692,536 would be generated. At a 68 percent collection rate, this would provide an estimated $470,924 in annual new revenues to the City.

---

[6]As we discussed earlier in this section and recommend in Section III.3, while we recognize that audits of these "escaped" businesses have yielded significant revenues, the Chief Auditor should experiment with simply requiring these newly identified businesses to complete back tax statements and pay based on their own calculations. It is not clear that full audits are required in all cases.

[7]The City of Los Angeles Tax Collector's Field Audit Unit reports that, among auditors devoted full-time to auditing, an average of 4 to 5 audits per month are completed.

[8]Productivity is not the only criterion on which Auditors and Principal Auditors should be evaluated. Standards of accuracy, thoroughness and fairness must also be evaluated.

[9]The key assumptions guiding the revenue estimates are: (1) Each auditor is at least capable of completing 26 audits per year (the FY1993-94 average, assuming the twenty person audit staff was reduced by five auditors who did administrative/ accounting work; (2) The average audit deficiency billing per audit would be $13,318, which was the inflation-adjusted FY 1990-91 average. (See Footnote No. 1.); (3) The reported eight year average collection rate of 68 percent of audited deficiency billings is correct, and could be maintained when audit deficiency collections are turned over to the new accounting staff in the Business Tax Division.

√ Hire the full complement of six new accounting/administrative staff in the Business Tax Division (as approved in the FY1994-95 budget), transfer administrative and accounting duties of the fourth audit team to these new personnel, and return the fourth audit team to full-time audit duties. At 26 audits per auditor per year, an additional 130 audits would be completed per year. Assuming average deficiency billings of $13,318 per audit, additional deficiency billings of $1,731,340 would be produced. At a 68 percent collection rate, this would provide an estimated $1,177,311 in annual new revenues to the City.

√ Require all auditors and senior auditors to complete the equivalent (in performance value) of 46 audits per year, instead of the 26 per auditor that was the FY1993-94 average. Assuming all auditors are devoted full time to audits, with the exception of two auditors still answering taxpayer telephone inquiries, 18 auditors would complete the equivalent of an additional 20 audits per year, or a total of 360 additional audits per year. These 360 additional audits would generate an additional estimated $4,794,480 in audit deficiency billings, and an estimated $3,260,246 in collections for the City.

However, the increased total annual volume of audits (from 386 to 746) would result in lower average per audit deficiency billings for the base level of 386 audits that the Audit Unit would complete even without productivity standards, particularly as the high yield delinquent and unregistered accounts are handled by the proposed Collections Division instead of the Audit Unit, and a portion of audits are selected for notoriety, rather than revenue maximization. After adjusting for reduced deficiency billings and collections in the base number of audits, the recommended increase in audit productivity would result in a net increase of approximately $1,314,183 in audit deficiency billings, and an estimated $893,644 in collections for the City.

In summary, the Audit Unit could generate an additional estimated $3.7 million in deficiency billings, which would produce an estimated $2.5 million in new revenue collections, by (1) reducing Auditor telephone assistance duties by 50 percent ($470,924 in annual collections); (2) returning the fourth team of Auditors to audit work ($1,177,311 million in annual collections); and (3) enforcing productivity standards to require all Auditors to complete the equivalent of 46 audits per year ($893,644 in annual collections).

INTERNAL CONTROLS

The United States General Accounting Office (GAO) manual on "Government Auditing Standards" states that establishing and maintaining an internal control structure is an important responsibility, "essential to achieving the proper conduct of government business..." and "serving as checks and balances against undesired actions." Although GAO standards do not specifically apply to tax audits, when government itself is performing an audit function, it is particularly

important to establish and enforce internal controls to assure taxpayers that they will be treated fairly. The Business Tax Division needs to improve internal controls in the areas of audit assignments and servicing of audited accounts.

Audit Assignments

The auditing staff of the Business Tax Division is now divided into four teams, each headed by a Principal Auditor. (One of the teams has been relieved of audit responsibilities in order to handle administrative matters, although the Chief Auditor plans to return them to auditing once the new accounting staff can take over these duties.) Each team selects and carries out audits of firms whose business names start with a particular portion of the alphabet. As of the writing of this management audit, the audit teams have had the same alphabetic assignments for at least four years.

The Chief Auditor has advised the Budget Analyst that he intends to institute a policy of regular rotation of the alphabetic audit assignments. The Budget Analyst endorses this reform, because rotation of audit assignments is one effective way to guard against unfair treatment (whether favorable or unfavorable) of particular business taxpayers. Audit team alphabetic assignments should be rotated every two years.

Servicing of Audited Accounts

The audit of business taxpayer accounts frequently results in deficiency billings: i.e. the taxpayer is found to owe more money than s/he paid at the time the taxes were due, and is assessed the balance, plus interest and penalty charges. Completion of an audit report that states the amount and reasons for any deficiency billings (or refunds to the taxpayer) should conclude an auditor's involvement with that account, other than to answer any questions about the content of the audit. However, under current practice, the auditor or his supervising Principal Auditor goes on to bill the taxpayer for the deficiency, make recommendations to the Chief Auditor about penalty waivers, set up time payment arrangements with the taxpayer if such are requested, make collection-related contacts with the taxpayer if payment is not forthcoming, and record all payments made to the account in the BTS system.

According to the Principal Auditors, if an audited account has not been paid in full after three to six months (there is no formal rule on the subject), the account is forwarded to the Investigations Division for further collection action. However, the Budget Analyst found two examples of audited accounts that were not forwarded to Investigations for collection for approximately one year. Investigators report payments back to the Principal Auditor, who is still responsible for updating BTS and ultimately closing the account. Investigations staff advised the Budget Analyst that they accept an Auditor's decision to close an account, even if, according to their records, the full amount of the deficiency billing has not been paid.

As discussed in Sections I.1 and IV.2, a consolidated Accounting Division should track all audited and delinquent accounts and mail initial audit deficiency bills. A dedicated Collections Division should eventually handle all collection efforts for the Tax Collector's Office, including collection of audit deficiency billings that are not paid voluntarily after the initial billings, and refer payments to the Accounting Division. Until such a reorganization is implemented, however, all servicing of audit deficiency accounts should be carried out by the new Accounting and Statements unit of the Business Tax Division, rather than by the Auditing Unit. The separation of auditing from collections will improve internal controls by providing a check and balance mechanism, minimizing the opportunities for unfair or biased application of tax compliance efforts.

SUMMARY

Auditors identify audit deficiencies for businesses that have not filed tax returns and/or have not registered with the City, when such unregistered/delinquent accounts should be pursued by a Collections Division. This practice cost the City $186,235 to $1,381,573 in uncollected revenue in FY 1993-94.

Audit productivity has declined substantially in the past three years, due to: (1) reduced accounting staff; (2) implementation of several legislative changes; (3) early retirements and long vacancies; and (4) coincidental implementation of the complex Business Tax System. Relieving auditors of taxpayer assistance ($470,924) and account maintenance ($1,177,311) duties would increase collected revenues from audited deficiencies by an estimated total of $1.6 million per year. The Business Tax Division has begun to implement this redirection of auditors to focus them on audit activities, and the decline began to reverse itself in FY 1993-94. Careful planning and budgeting for implementation of changes in tax regulations by the Tax Collector and the Board of Supervisors, and implementation of our recommendations for automation training and communications would also increase audit productivity. Development and enforcement of productivity standards to achieve an average of one audit completed weekly by each auditor would further increase collected revenues by an estimated $1 million. Total potential revenue increases of an estimated $2.8 to $4 million annually are identified in this section.

Selection of which firms the Tax Collector audits has been carried out on an ad hoc basis, without careful prioritization. While the Business Tax Division is in the process of implementing an automated selection system, the Division needs to study historical data to refine selection criteria. The Business Tax Division should also improve internal controls in the areas of audit assignments and account servicing.

RECOMMENDATIONS

The Chief Auditor should:

1. Refer delinquent and unregistered business accounts to the Collections Division proposed in Section IV.2, rather than the audit unit of the Business Tax Section.

2. Develop a routing system to send a large proportion of telephone inquiries to Taxpayer Services and or Accounting, thereby reducing auditor telephone duties by 50 percent. This, combined with the recent establishment of a regular staffing for Taxpayer Services, would provide an additional 2 FTEs of auditor time for audits.

3. Require auditors to log time spent on telephone taxpayer assistance after installation of the voice mail system. Use these logs to compare the cost to the City in lost audit revenue with the cost of hiring appropriate personnel to answer telephone questions.

4. Return the team of auditors now assigned to administrative duties to full time, regular audit duties as soon as the new accounting staff can be trained to take over their administrative/account maintenance duties. This would provide an additional 5 full time auditors.

5. Develop and enforce auditor performance standards requiring all auditors to complete the equivalent (in performance value) of 46 audits per year, instead of the 26 per auditor that was the FY1993-94 average.

6. Refine the new automated audit selection process to make full use of available information. Audit selection should reflect the Tax Collector's priorities in terms of the number selected for their revenue potential, and the number selected to achieve audit notoriety by auditing a representative sampling of business types. The automated process should be designed to select a realistic number of audits, taking into account that a projected (and limited) number of escaped business audits, delinquent account audits and other special purpose audits will also be required during the year.

7. Institute a practice of rotating audit team alphabetic assignments every two years, for internal control purposes.

8. Assign all servicing and account maintenance of audited accounts to the Accounting and Statements Unit (and eventually to the Accounting and Collections Divisions). Such activities should no longer be carried out by auditors, to provide a check and balance mechanism that will minimize the opportunities for unfair or biased application of tax compliance efforts.

The Tax Collector should:

9. Establish a step-by-step guideline for actions to be taken on delinquent accounts, depending upon the size of the account. Control referral of delinquent accounts for audit so that (1) all non-litigation collection activities are pursued before an audit is commenced; and (2) the total number of delinquent account audits per year is limited to provide balance and variety in the audit program.

10. Establish a policy regarding the balance between the audit goals of revenue maximization and encouragement of voluntary business taxpayer compliance. This will establish the proportion of audits to be selected for their collection potential, and the proportion to be selected by business type to gain wider public awareness of the audit program.

The Board of Supervisors should:

11. Request a written analysis from the Tax Collector of any proposed tax ordinance, both in terms of the Tax Collector's assessment of the ordinance's impact on taxpayers and revenue collection, and in terms of the Tax Collector's estimate of required staffing and impacts on the day-to-day operations of the Department.

COSTS/BENEFITS

Revenue for FY 1993-94 would have been $186,573 to $1,381,573 higher if delinquent and unregistered business accounts had been referred to a Collections Division instead of referred to the Auditing Unit of the Business Tax Division. The Auditing Unit of the Business Tax Division will increase audit deficiency collections by an estimated $1.6 million per year by limiting auditor taxpayer assistance duties to 2 FTE auditors, instead of the current 4 FTE auditors, and returning the team of auditors who have been assigned to full time accounting and administrative duties to full time auditing.

Developing and enforcing productivity standards to require each auditor to complete the equivalent (in performance value) of 46 audits per year would increase collections by an estimated $1 million per year, resulting in a total revenue benefit from our recommendations of an estimated $2.8 to $4 million annually.

New staff costs, to be determined by the Tax Collector, would be incurred if the Chief Auditor's analysis of telephone taxpayer service activities by auditors shows that additional accounting staff should be hired to perform this function, so that auditors can focus on auditing activities. However, such costs would be more than offset by additional audits being conducted, resulting in increased audit deficiency billings and collections.

SECTION III.2: REVIEW OF CITY PARK AUDIT

The Budget Analyst's review of an audit conducted by the audit staff of the Business Tax Section of the Tax Collector's Office found that audit staff: (1) used methodology that is not supported by work papers, which resulted in an audited deficiency billing that was $35,574 less than if the existing methodology developed by the City's Department of Public Works (DPW) had been used; and (2) neglected to assemble the complete working papers necessary to establish an audit trail, to permit thorough supervision by senior staff auditors and to permit review by any experienced auditor.

BACKGROUND

In February of 1994, the Audit Staff of the Business Tax Section of the Tax Collector's Office began conducting an audit of San Francisco Parking, Inc. (City Park), which has parking operations at Candlestick Park. The Tax Collector conducted the audit to verify that City Park was paying all taxes due the City. Because the audit of City Park was a high priority, complex case, we have selected it for review of the methodology and procedures used in conducting audits of business taxpayers.

The Budget Analyst's review of the audit conducted by the audit staff of the Business Tax Section of the Tax Collector's Office found that audit staff: (1) used methodology which resulted in lower audited deficiencies billed to the auditee; and (2) neglected to assemble the complete working papers necessary to establish an audit trail and to permit thorough supervision by senior staff auditors.

Summary of Tax Collector's Audit Purpose and Findings

City Park operates and maintains the main stadium lot as well as twelve peripheral lots at Candlestick Park during the football season, and 32 additional garages and parking lots garages throughout the City. City Park also manages three garages and lots in downtown San Francisco which are owned by the Golden Gate Parking Company.

The Tax Collector, according to page one of the Business/Payroll Tax and Parking Tax Audit for Calendar Years 1991, 1992, and 1993, "completed a business tax, payroll expense tax, parking tax, and financial and compliance audit of San Francisco Parking, Inc. for the period of January 1, 1991 to December 31, 1993. As stated in the final audit report, the purpose of the audit was to determine:

- The fairness and accuracy of the taxpayer's returns filed with the City and County of San Francisco;
- The adequacy and reliability of the taxpayer's internal accounting and administrative controls; and
- Whether the taxpayer complied with the City's business tax, payroll expense tax and parking laws and regulations.

The audit document states that "[t]he audit was performed in accordance with generally accepted auditing standards," and goes on to specify those standards under the Scope and Review of Internal Accounting and Administrative Controls sections of the Tax Collector's report. This language, which is derived from the Federal General Accounting Office's Government Auditing Standards, specifies that the audit meets certain standards, by which any informed reviewer should be able to trace and recreate the audit conclusions. Thus, our review was conducted on the assumption that we could use the audit work papers to trace and affirm the Tax Collector's audit conclusions.

The Tax Collector's audit concluded that City Park has adequate controls for the downtown facilities, but needs to improve internal controls significantly for the lots located at Candlestick Park. The audit also indicated that parking revenues were under-reported for the Candlestick Park facilities. The under-reporting of revenue at Candlestick Park facilities resulted in the underpayment of parking taxes owed to the City. Finally, the audit findings indicated that there was also a problem of underpayment of parking taxes on the City Park downtown garages and lots. The Tax Collector billed and City Park has now paid the $94,884 of audited deficiencies and the associated penalties and interest.

ESTIMATED AVERAGE NUMBER OF PASSENGERS PER VEHICLE

The Budget Analyst does not agree with the Tax Collector's methodology to determine the number of cars parked at Candlestick Park, and the consequent parking tax owed by the auditee. Specifically, the Tax Collector estimated the number of vehicles parked at Candlestick Park by modifying the methodology developed by the Department of Public Works (DPW) in a 1985 traffic flow study. We believe that the DPW's methodology is superior to the modified methodology used by the Tax Collector. Furthermore, the Tax Collector's work papers do not provide a clear record by which his methodology can be recreated. The following paragraphs describe the DPW's methodology, the Tax Collector's methodology (for

which we did not find clear support in the working papers), and the Budget Analyst's evaluation of the two methodologies.

Standard audit procedures could not be used to determine the number of vehicles parked at Candlestick Park, because City Park did not have adequate records for their Candlestick Park facilities, such as numbered parking stubs, which would permit direct verification of their tax statements. (The Controller's Office had previously recommended use of numbered stubs for City Park.) Therefore, to verify the tax statements submitted by City Park, the Tax Collector's auditors had to estimate the number of vehicles that paid for parking in City Park lots at Candlestick Park during the audit period.

In 1985, the DPW conducted a traffic flow study of Candlestick Park, which was used by the Department of Parking and Traffic (DPT) to prepare a 1988 "Candlestick Park Transportation Improvement Plan." The cornerstone of this traffic flow study were surveys which indicated that 81.1 percent of Candlestick Park attendees arrived by car, and that the average ridership per car was 2.67 persons. These estimates were based on the following:

- A vehicle count from an aerial photograph for an October 13, 1985 game, adjusted to subtract a vehicle-count from a non-game day (in other words, adjusted to accommodate neighborhood cars); and

- Turnstile-based attendance for September 26, 1985, adjusted to subtract persons who used public transit, charter, buses, taxi, auto drop-off, and walking from home, calculated based on information from SamTrans, the San Francisco Municipal Railway, and observations.

The DPW confirmed its estimates by comparing adjusted turnstile-attendance to a vehicle count based on the number of parked vehicles reported by City Park. This confirmation estimate supported the 2.67 passengers per vehicle estimate noted above. Also, in 1989 and in 1990, the DPW conducted an actual vehicle count by recording the number of passengers in a sample of 200 vehicles at Candlestick Park on a game day. This vehicle count estimated 2.4 and 2.6 average passengers per vehicle in 1989 and 1990, respectively.

The Tax Collector's audit staff estimated the average number of passengers per vehicle to be 2.73, a 2.3 percent increase, using a method "based on the DPW traffic flow study of 1985 and a City Planning report of 1988 on Candlestick Park." (The City Planning report estimates the percent of buses, autos, and campers, based on the October 13, 1985 aerial photograph.) The Tax Collector's auditors adjusted the DPW methodology as follows:

- An updated vehicle count, based on an aerial photograph from October 13, 1985, adjusted to subtract non-game related vehicles. This adjustment includes subtracting 3,288 vehicles which were said to be employees of Tuntex, a business located near Candlestick Park. Tuntex is open for business during the hours of 9 to 5, Monday through Friday. October 13, 1985 was a Sunday.

- Turnstile-based attendance for October 13, 1985, the same day as the aerial photograph, adjusted to subtract a larger percentage of persons using public transit than the DPW's estimates, and to subtract the same number of persons using charter buses, taxi, auto drop-off, and walking from home.

- An assumption that carpooling has increased since 1985, thereby increasing the average number of passengers per vehicle.

The Tax Collector believes that his methodology is superior to the DPW's, because the vehicle-to-passenger ratio is calculated using a same-day vehicle count and attendance count. While we agree that the DPW's methodology is flawed in that the ratio is estimated using different dates for the vehicle count versus the attendance count, the DPW's support methodologies — which, as noted above, include actual vehicle and passenger counts for two calendar years showing an even lower ratio than the DPW originally estimates — provide additional support for their lower estimate. We believe that the Tax Collector has overestimated the average number of persons per vehicle, because:

- The Tax Collector's work papers do not show adequate justification to subtract 3,288 vehicles on the assumption that these vehicles belong to Tuntex employees, especially given that Tuntex employees do not typically work on Sundays;

- The Tax Collector's work papers do not show adequate justification to assume a higher number of persons used public transportation during the audit period than in 1985; and

- The Tax Collector's work papers do not show adequate justification to assume that a higher number of persons carpooled during the audit period than in 1985.

The Tax Collector's auditors assumed that 80 percent (rather than 81.1 percent) of Candlestick Park attendees arrived by car, and that the average ridership per car was 2.73 persons (rather than 2.67 persons). When applied to turnstile attendance during the three year audit period, these adjustments result in a parking estimate of 16,170 fewer cars for the 24 regular season games than would the original DPW variable values as determined by the survey. Use of the original DPW values would have generated an additional $177,870 in revenue (16,170 cars x $11.00 per car) which is equivalent to $35,574 in additional parking taxes, at the tax rate in effect during the audit period.

As a result of our examination of the Tax Collector's audit of City Park, the Chief Auditor directed his staff to complete a new survey of parking at Candlestick Park football games. According to the Chief Auditor, this survey supports the Tax Collector's revisions of the DPW assumptions. However, this survey was carried out

after the audit of City Park was completed. Had the survey failed to support the revisions, it would have been too late to revise the audit deficiency billing.[1]

FAILURE TO ASSEMBLE ADEQUATE WORK PAPERS

As noted above, the Tax Collector's audit report of City Park states that Generally Accepted Government Auditing Standards (GAGAS) were used in the performance of this audit. Upon review, the Budget Analyst has determined that two of the standards were not met. The standard which were not met require that: (1) due professional care be used in conducting the audit and preparing related reports; and (2) working papers should contain sufficient information to enable an experienced auditor, having no previous connection with the audit, to ascertain from them the evidence that supports the auditor's significant conclusions and judgments. This portion of our review was conducted in consultation with a Certified Public Accountant, who reviewed the work papers submitted to the Budget Analyst's Office.

Financial audits must contain cross-references indexing all audit findings to work papers. Without such cross-references, no audit trail exists. Creating the audit trail serves as a final quality control measure ensuring that all audit findings are supported by the work papers, and that all work papers are relevant to the audit. The Tax Collector's City Park audit contained no such cross-references. As a result:

(1) We were unable to identify support for the findings and methodologies contained in the audit (as with the Tax Collector's estimated average number of passengers per vehicle);

(2) Certain work papers appeared to be missing. For example, the final audit report prepared by the Tax Collector's audit staff refers to trial balances, Federal tax returns and California State tax returns. Upon examination of the working papers, we found that the working papers did not include tax returns for any of the three years audited. Trial balances were also not included in the working papers for the last year of the audit period, 1993. The audit staff indicated that the tax returns for the last year of the audit period, 1993, were not available and were not reviewed as part of the field work for this audit, and that certain tax return documents were examined but not copied. If this information was relevant to the audit, it should have been indexed and included in the work papers; and

(3) We were unable to evaluate the relevancy of the work papers provided to us by the Tax Collector's Office. In fact, the Tax Collector's audit staff indicates that the tax forms and trial balances were immaterial to the audit findings. If this information was <u>not</u> relevant to the audit, it should not have been

[1]We have not examined the after-the-fact survey methodology used by the Business Tax Division in carrying out this post-audit survey, because this was immaterial to our consideration of the quality of the audit.

mentioned in the audit report, because any information mentioned in the audit report should be supported by work papers.

The presence of calculation and transposition errors identified by the Budget Analyst provided further evidence that completing the mandatory cross-referencing would have provided necessary quality control. Although these errors do not materially effect the audit outcome, they should have been detected and corrected prior to the completion of the audit, and would likely have been detected through the cross-referencing process.

CONCLUSIONS FROM CITY PARK AUDIT REVIEW

The problems identified in this review of a major audit conducted by the Business Tax Section underscore the need to establish uniform procedures to be used in conducting all audits. Auditors in the Business Tax Division are provided with a manual on "Audit Approach and Procedure Guidelines," as well as a set of three "Audit Program Checklists" (for small/simple audits, intermediate audits, and complex audits). The existing procedural guidelines for auditors are helpful, but do not provide clear policies regarding acceptable documentation, working papers and tests of reasonableness. Nor do they address issues such as handling of challenges to audit methodology or conclusions, and standards for audit review and supervision.

The Chief Auditor should direct the 1822 Administrative Analyst (a new position in FY 1994-95) to assemble sample audit policies and procedures manuals from the IRS and other cities, as well as to consult the GAO manual of Government Auditing Standards. These examples can be used to revise and enhance the existing procedural guides.

Once established, these audit procedures should be presented to the Tax Collector's audit staff in a forum which encourages the audit staff to ask questions and exchange ideas regarding the implementation of the new procedures. After the initial training, the Tax Collector's audit staff should receive on-going training in audit procedures. This training should occur, at a minimum, on a biennial basis.

The Chief Auditor should also direct the Administrative Analyst, or one of the Principal Auditors, to maintain a central manual of administrative decisions and case law related to San Francisco business taxes. The person responsible for this manual should provide each auditor with an annotated index of its contents, to be updated as necessary.

The Audit Unit has four Principal Auditors. These four positions have minimal direct audit responsibilities; their responsibilities are primarily supervisorial. The Chief Auditor should evaluate the Principal Auditors annually based on both the productivity of their audit team (See Section III.1), and the quality of the audits completed by the team. The Chief Auditor should review a random sample of audits (and accompanying working papers) from each audit team each year as part of the evaluation of Principal Auditors.

SUMMARY

Review of an audit conducted by the audit staff of the Business Tax Section of the Tax Collector's Office found that audit staff: (1) used methodology that is not supported by work papers which resulted in an audited deficiency billing that was $35,574 less than if the existing methodology developed by the City's Department of Public Works (DPW) had been used; and (2) neglected to assemble the complete working papers necessary to establish an audit trail and permit thorough supervision by senior staff auditors.

RECOMMENDATIONS

The Tax Collector's Chief Auditor should:

1. Bill City Park for an additional $35,574 plus penalties and accrued interest.

2. Direct the 1822 Administrative Analyst to assemble sample audit policies and procedures manuals from the IRS and other cities, as well as to consult the GAO manual of Government Auditing Standards. Direct this staff person to revise and enhance the existing audit procedural guides, and present the new guides to audit staff in a form which encourages the exchange of ideas regarding the implementation of the new procedures.

3. Provide auditors with ongoing in-house training in audit procedures, at least on a biennial basis.

4. Direct the Administrative Analyst or a Principal Auditor to maintain a central manual of administrative decisions and case law related to San Francisco business taxes. The person responsible for this manual should provide each auditor with an annotated index of its contents, to be updated as necessary.

5. Include an evaluation of the quality of audits performed by each audit team in the annual performance evaluation of the Principal Auditors who supervise the teams. Review a random sample of audits (and accompanying working papers) from each audit team each year as part of the evaluation process.

COSTS/BENEFITS

The proposed recommendations involve allocation of time on the part of existing employees of the Tax Collector, and are expected to result in improved audits of business taxpayers, which should lead to more accurate audit deficiency billings.

SECTION III.3: BUSINESS REGISTRATION

There is no unit of the Tax Collector's Office with clear responsibility for registering businesses, although the Business Tax and Investigations Division make limited attempts to identify unregistered businesses. To estimate the portion of unregistered business in San Francisco, the Budget Analyst visited five commercial buildings. Based on the data collected and verified by the Tax Collector's Office, of the 359 businesses surveyed, a total of 206 (57%) were registered with the Tax Collector and 153 (43%) were not registered. Combining this survey with other estimating methods, all of which are understated and overstated in different ways, the number of unregistered firms doing business in San Francisco might be as low as 9,000 or as high as 53,000. As a result, the Budget Analyst estimates that the City loses up to $6.8 million annually in business registration fees. Assuming that these unregistered businesses also owe the average annual Gross Receipts and Payroll Taxes paid by businesses to the City, a conservatively estimated additional $14.3 million annually in such taxes would be lost.

The Tax Collector should establish a Business Identification Unit in the Business Tax Division, with responsibility for identifying and registering businesses. This Business Identification Unit should work with City Departments, the Chamber of Commerce and other branches of government to identify all businesses operating in San Francisco.

The Business Identification Unit should track all identified businesses to ensure that they actually register with the City. Those that may owe Payroll and Gross Receipts Taxes should be required to submit tax statements and payments.

As part of this management audit, we reviewed the Business Registration process in the Tax Collector's Office. The purpose of this review was to determine whether the Tax Collector is identifying businesses that must register and enforcing the registration requirement for all businesses. Efficient identification of businesses and equal enforcement would maximize revenue and ensure equity.

Our review of the Business Registration process included identifying:

√ the activities performed by the Tax Collector in regard to Business Registration;

√ the units within the Tax Collector's Office with responsibility for business registration-related activities;

√ techniques that could be used to identify more unregistered businesses;

√ current practices regarding collection of business registration fees and business taxes from previously unregistered businesses;

√ recommendations for increasing the identification and registration of previously unregistered businesses, and improving collection of fees and taxes due from such businesses.

To measure the extent to which businesses fail to register, we took cluster samples of businesses (that is, all of the businesses located within specific large buildings) and compared the businesses within the cluster sample with the Tax Collector's list of registered businesses. We also compared the number of businesses having fictitious business names on file with the County Recorder and the number of businesses with advertisements in the Nynex Yellow Pages with the Tax Collector's list of registered businesses.

We found that the Tax Collector has not established clear accountability for Business Registration within his own office, that the City has not established procedures that require all businesses who contact the City to register, that a large percent of businesses are not registered, and that the Tax Collector has not maximized available resources to identify businesses. We also found that, for those unregistered firms that are identified, it is the practice of the Business Tax Division to audit all accounts for which it is apparent that Payroll/Gross Receipts Tax will be due. Although this practice boosts auditor's statistics, it is not necessarily the most efficient approach to collecting back taxes from previously unregistered businesses.

This section of our report does the following:

- provides background on Business Registration, including costs, number of registered businesses, and revenue;
- summarizes the Business Registration process, from the point of view of a business as well as within the Tax Collector's Office;

- estimates the extent to which businesses do not comply with the City's Business Registration requirements, and the amount of revenue lost through lack of compliance; and
- establishes specific recommendations for:
  - √ creating accountability within the Tax Collector's Office for Business Registration;
  - √ ensuring that all businesses who must contact the City for any reason are required or guided toward Business Registration; and
  - √ maximizing the use of City and other resources to identify businesses.

BACKGROUND

The Tax Collector's Office collects a business registration fee from all enterprises operating in San Francisco. The amount of this fee is currently $25 to $500, depending on the gross receipts of the business. The FY 1994-95 budget includes $7,764,000 in projected Business Registration Fee revenues. Currently, approximately 60,000 businesses are registered with the Tax Collector.

The Business Registration Fee serves not only as a source of revenue, but also as a means to establish a list of businesses that must file San Francisco tax returns for the Gross Receipts and Payroll Tax, Hotel Taxes, Parking Taxes, Utility User Taxes and other taxes collected by the Tax Collector's Office. For example, the Tax Collector collected an average of $12 of Gross Receipts and Payroll Taxes for every $1 of Business Registration Fees collected.

IDENTIFICATION OF BUSINESSES

Current Practices

The Process Outside the Tax Collector's Office

Any business that opens in San Francisco, or begins to do work in San Francisco, is supposed to register with the Tax Collector and obtain a Business Registration Certificate. Currently, certain City services are withheld from businesses until they show proof that they have registered with the Tax Collector. Withholding services is a good method of encouraging payment, according to a February, 1994 General Accounting Office survey of 43 states.[1]

[1]United States General Accounting Office, Tax Administration: State Tax Administrators' Views on Delinquent Tax Collection Methods. Fact Sheet for the Chairman Subcommittee on Oversight, Committee on Ways and Means, House of Representatives. February, 1994.

A business may not record a fictitious business name with the County Recorder's Office or receive a residential parking permit until they have shown a copy of their Business Registration Certificate. However, in some cases, businesses are permitted to receive City services without producing a copy of their Business Registration Certificate. For example, a business can register as a disadvantaged business with the Human Rights Commission without showing proof that it has registered with the Tax Collector's Office.

Business Registration Process: Inside the Tax Collector's Office

No single Section of the Tax Collector's Office has responsibility for administering the Business Registration. In summary:

- *The Business Tax Division* is responsible for maintaining a database and implementing billings. This responsibility includes accepting registration forms over the counter and through the mail, and performing data entry of address changes, business status, and payments. The goal of the Business Tax Division, in regard to business registration, is to assist customers in completing registration forms and to process all such forms that the Division receives.
- *The Business Tax Division, Audit Unit* is the only area of the Tax Collector's Office with responsibility for identifying unregistered businesses. The Audit Section is divided into three teams. Each team has one auditor assigned, part-time, to identifying businesses through the telephone book and address checks. However, these auditors are not charged with designing and implementing a comprehensive business identification effort; instead, they identify businesses in order to audit them. Their focus is to bill for unpaid Payroll and Gross Receipts Tax, not to identify unregistered businesses. We estimate that the Audit Unit identifies less than 100 unregistered businesses per year.
- *The Investigations Division, Clearance Unit* is responsible for checking on whether firms that have applied for Business Registration Certificates owe the City Business Taxes or Property Taxes. The Clearance Unit notifies registrants and withholds Business Registration Certificates until payment for any taxes owed is received by the Tax Collector.
- *The Investigations Division* has added three new Collection Officers as of FY 1994-95. These new Collection Officers have been given responsibility, in part, for performing "survey" work to identify businesses that have not registered. However, this activity remains a low priority for the Investigations Division.

Investigators are, in theory, supposed to conduct spot checks for business registration as they do field collection work, but in practice, few unregistered firms are identified by the Investigations Division. In addition, the Investigations Division is responsible for collections activities related to Business Registration. However, pursuing delinquent business registration fees is a low priority for the Investigations Division.

Neither the Business Tax Division nor the Investigations Division claims accountability for identifying all businesses operating in San Francisco. Throughout this audit, we had difficulty locating the parties accountable for the various aspects of Business Registration. Clearly, within and between divisions, there is a lack of awareness regarding responsibility and activities surrounding Business Registration. No central authority establishes performance goals, priorities, or standards for Business Registration-related activities, and, as a result, the Tax Collector is unsuccessful in identifying businesses, processing information,[2] and collecting delinquent Business Registration revenues efficiently and effectively. The following paragraphs estimate the number of businesses that have not registered with the Tax Collector.

Estimated Number of Unregistered Businesses in San Francisco

Since no one in the Tax Collector's Office has accountability for Business Registration, and since neither the Business Tax Division nor the Investigations Division have established identification of unregistered businesses as a priority, many San Francisco businesses may have not been identified. For each business that should register but does not, the annual registration fee of $25 to $500 is lost each year. In addition, approximately ten percent of businesses pay a Business Tax. Thus, an estimated ten percent of businesses that do not register are also avoiding payment of the City's annual Business Taxes. The following paragraphs estimate the number of businesses that have not been identified by the Tax Collector's Office, and the amount of revenue lost because the Tax Collector has not identified them.

To estimate the portion of unregistered businesses in San Francisco, we visited five commercial buildings and, using the directory on the ground floor, obtained a list of businesses at that site. We compared this information with the Tax Collector's list of registered businesses to determine the number of registered versus unregistered businesses at each site.[3] We visited five commercial buildings to conduct this sample, as follows: one in China Basin; three sites South of Market; and one downtown. We then worked with the Tax Collector's Office, which reported that a more accurate representation of businesses is maintained by the lessor of each building and the Tax Collector's staff obtained listings from each of the lessors of these same five commercial buildings.

---

[2]In Section I.1 of this report, we discuss the Business Tax Section's lack of success in processing changes of address.

[3]We compared this information in two ways. First, we sorted the Tax Collector's listings by street address to find all registered businesses located at a particular site. Second, because a business's mailing address may be different from its location, we sorted the Tax Collector's listings by business name.

Based on the data secured by the Tax Collector's Office, we found that, of the 359 businesses selected, a total of 206 (57.38 percent) were registered with the Tax Collector, and 153 (42.61 percent) were not registered. Based on an average registration fee of $127, the Tax Collector loses $19,431 annually in registration fees alone for these 153 unregistered businesses, identified through our sample survey. Also, these unregistered businesses may owe Gross Receipts or Payroll Taxes, but only registered businesses pay business taxes, such that the City is losing additional significant revenues. Table 1 below details the location of the businesses and the percentage of registered businesses at each location.

Table 13

Percent of Registered Businesses by Location

Location	Number of Eligible Businesses	Number of Registered Businesses	Percent of Registered Businesses
369 Pine St.	56	26	46.43%
American Industrial Center (2325, 2331, 2339, 2345, 2455, 2505, 2565, 2573 3rd St.)	166	87	52.41%
660 3rd St.	15	14	93.33%
665 3rd St.	67	40	59.70%
185 Berry St.	55	39	70.91%
Total	359	206	57.38%

Our sample is not representative: it is not random, and it does not include businesses located in a facility other than a large office building, any businesses that are in the outlying neighborhoods of the City, or any businesses that are not located in the City but do business here. Therefore, we cannot assume that 42.6 percent of all San Francisco businesses are not registered with the Tax Collector. However, our sample includes service, retail and manufacturing establishments. Furthermore, the building with the lowest rate of registered businesses among those sampled was located at the intersection of Pine Street and Montgomery Street, a prominent downtown location. Other businesses, located in less central locations of the City, may in fact have an even lower registration rate than our sample indicates.

Table 1 above presents the results of an analysis that gave the benefit of the doubt to the businesses and the Tax Collector's Office, by omitting the many unregistered firms that were listed in building directories but not on the lessor's list of building tenants. The Budget Analyst's original methodology, based on the directory on the ground floor of these office buildings, identified an even lower business registration rate than reflected above. For example, at the 369 Pine Street location, the Budget Analyst identified a total of 85 businesses, (rather than the 56 businesses based on the lessors data as reflected above) and found a registration rate of 31 percent (as opposed to 46.4 percent), or 69 percent unregistered

businesses. To confirm our survey, the Budget Analyst conducted a follow-up telephone survey of these 29 additional unregistered businesses (85 directory business listings less 56 lessor business listings). The Budget Analyst was able to contact 15 of the 29 businesses and all reported that they were located at the 369 Pine Street address, however, most of these unregistered businesses indicated that they were subleasing their space, the probable reason for their omission from the lessor's lists. Conservatively, adding only the 15 contacted unregistered businesses results in a registration rate of 37 percent for this one location. In other words, based on our conservative estimates, 63 percent of the businesses located at this one Pine and Montgomery Street location in downtown San Francisco are not registered with the Tax Collector's Office. This reexamination of the data collected also identifies serious flaws in the methodology used by the Tax Collector's Office to identify businesses in the City, because use of lessor building data may not include sublease tenants.

To obtain another estimate of the number of businesses in San Francisco, we contacted the Recorder's Office to ascertain the number of businesses that have fictitious business name statements on record. Approximately 66,000 businesses currently have a fictitious business name on file with the Recorder's Office. This number understates the total number of businesses that should register with the Tax Collector, in that: businesses operating under the owner's name need not file a fictitious business name statement; some businesses operating under a fictitious business name may not file that name with the Recorder's Office; and some businesses operate in San Francisco but are headquartered outside of the City and have filed their fictitious business name statement in other jurisdictions. However, the number may overstate the total number of businesses since the list may include defunct businesses: a business may not notify the Recorder's Office when it has gone out of business; and some businesses with fictitious business names may be exempt from registering with the Tax Collector's Office (e.g., non-profit businesses).

We also contacted Pacific Bell to ascertain the number of businesses with listings in the Pacific Bell white pages. However, Pacific Bell was able to provide only Statewide information indicating that 2.1 million businesses hold accounts with Pacific Bell in California. We did not extrapolate from this information to San Francisco based on population because San Francisco has a substantially higher proportion of businesses than most California jurisdictions.

Finally, according to the Nynex Yellow Pages, there are 110,000 business advertisements in the Yellow Pages. However, this number does not reflect the number of San Francisco businesses. It overstates the actual number of businesses because: some businesses may obtain more than one advertisement; some businesses operating outside of the City advertise in the San Francisco Yellow Pages; and some businesses are non-profit, and thus exempt from the registration requirement. It understates the actual number because many businesses do not advertise in the Yellow Pages.

The following table shows the number of registered businesses as compared with the number of businesses in San Francisco, according to the above estimates.

Table 14

Estimated Number of Unregistered Businesses According to Various Estimated Numbers of San Francisco Businesses

Estimator	Current # of Businesses Identified by this Estimator	CY 1994 # of Businesses Registered by Tax Collector	# of Unregistered Businesses Under This Estimator	Lost Revenue Based on $127 Per Registration*
Survey of Office Buildings	98,600**	56,624	41,976	$5,330,952
Fictitious Business Names on File with County Recorder	66,000	56,624	9,376	1,190,752
Advertisements in Nynex Yellow Pages	110,000	56,624	53,376	6,778,752

*$127 was the average cost per registration for CY 1994 (total registered businesses = 56,624; total revenue = $7,193,827

**Assumes that 56,624 represents 57.4 percent of the total registered businesses

As the above chart indicates, the total estimated amount of lost revenue from unregistered businesses ranges from approximately $1.2 million to $6.8 million. In addition, in Calendar Year 1994, for each dollar the Tax Collector collected from Business Registration fees, the Tax Collector collected $12 from Gross Receipts and Payroll taxes.[4] Thus, based on lost revenue from Business Registration fees noted in the above table, the Tax Collector has also lost a maximum of $14.3 million to $81.3 million annually in additional Business Taxes owed by unregistered businesses. Together, this results in an estimated total annual loss of revenue to the City's General Fund of $15.5 million to $88.1 million. The amount of Business Taxes lost, however, is likely to be lower than these estimates, since larger businesses are easier to identify and therefore more likely to be in compliance with the Tax Collector's registration requirements. Unregistered businesses would tend to be smaller firms, owing lower Gross Receipts and Payroll taxes on average.

[4]The Tax Collector collected $69,891,411 from 7,583 businesses paying Payroll Taxes and $11,490,110 from 3,081 businesses paying Gross Receipts tax for CY 1993. The Tax Collector collected CY 1994 Business Registration fees at the same time he collected CY 1993 Business Taxes.

Recommended Practices

The Tax Collector should establish a Business Identification Unit in the Business Tax Division. This Unit should be staffed with an 1832 Management Analyst. The Management Analyst would be responsible for designing programs to identify businesses, educating businesses regarding their responsibility to register, and following up to ensure that all identified businesses do, in fact register with the City. The Management Analyst's activities might include:

- ***Matching lists of businesses retained by other departments to unregistered businesses***

  Many City departments possess databases listing businesses. For example, the County Recorder's Office maintains a comprehensive list of fictitious business names and addresses. (As noted above, businesses must now show proof of registration prior to recording a fictitious business name; however, this requirement was instituted on January 1, 1993. All businesses that recorded their fictitious business names prior to that date were not required to register by the Recorder, and should be pursued.) Other examples of departments with lists of businesses include the Human Rights Commission, the Mayor's Office of Economic Development, and any City department that issues renewable licenses (see Section II.1 of this report for information on licensing).

- ***Developing information exchanges with other branches of government***

  The Business Identification Unit should develop information exchanges with the State Board of Equalization, the Employment Development Department, the Franchise Tax Board, and the Internal Revenue Service, if possible. (The State Board of Equalization currently provides a comprehensive list to the City's Controller of all San Francisco businesses that pay sales tax to the State. The Identification Unit should use this list to identify additional businesses. Our survey of other jurisdictions showed that most use this tool to identify unregistered firms.)

  In regard to the Federal Internal Revenue Service (IRS), the IRS is empowered to provide lists of businesses filing Schedule C - Profit or Loss From Business forms to entities that collect income taxes. The IRS is currently determining whether the gross receipts tax collected by the City of Los Angeles qualifies as an income tax. If so, the IRS and the City of Los Angeles will begin negotiating an information exchange, under which the IRS would provide to the City the names and addresses of all entities within Los Angeles that filed Schedule C forms.

  San Francisco's gross receipts tax is modeled on the gross receipts tax in the City of Los Angeles. The Identification Unit should request that the IRS determine whether San Francisco's gross receipts tax qualifies as an

income tax.[5] If the IRS determines that the City's gross receipts tax qualifies as an income tax, the City should negotiate an information exchange with the IRS, wherein the City receives a list of all San Francisco businesses filing Schedule C forms. Such a list would not include entities doing business in San Francisco with out-of-City addresses, but it would provide a comprehensive list of San Francisco-based businesses.

- ***Proposing legislation to assist in identifying businesses***

  The Business Identification Unit could identify all points at which a business might require City services, and design appropriate legislation requiring businesses to show proof of registration prior to receiving such services. Other useful legislation might include requirements that landlords provide the names and addresses of new commercial tenants, or requirements that contractors provide the names and addresses of sub-contractors prior to receiving construction permits.

- ***Working with the Chamber of Commerce***

  The Business Identification Unit can establish contact with the Chamber of Commerce, and use this contact to educate businesses by distributing information fliers, making presentations, or accessing mailing lists to send informational notices.

- ***Developing information exchanges with commercial property owners and managers***

  The Assessor's rolls indicate whether a property is used for commercial purposes, and the number of rooms/units per property. The Business Identification Unit can use this information to contact commercial property owners, who can provide the names and addresses of commercial renters. (The Business Tax Division's Auditors have already established certain limited information exchanges with commercial property owners and managers.)

The cost of the new 1832 Management Analyst coordinating the Business Identification Unit should be more than offset by the new revenues from increased Business Registration fees. Assuming an annual cost of $75,000, including salary and fringe benefits, and a typical registration fee of $127, the Management Analyst would need to identify an additional 590 businesses each year to justify the position. It is likely that, initially, it will be easy to identify unregistered businesses. However, as the population of unregistered businesses shrinks, identifying such businesses will become more difficult. To ensure that the 1832 Management Analyst is fully supported by Business Registration fees, the Tax Collector should be required to demonstrate annually to the Board of Supervisors that the position has identified an increment of 590 additional businesses each

[5] This can be accomplished by contacting Ms. Susan Hernandez, IRS Disclosure Officer, at (213) 894-5504.

year, beyond the number of new businesses that would typically be identified by the Tax Collector's Office.

We anticipate that the position would eventually be unable to identify 590 new businesses, because the position will establish systems that ensure the automatic identification of businesses. At such time as this position no longer identifies at least 590 new businesses annually, the position should be eliminated.[6]

(As noted above, some portion of the new businesses would likely owe other business taxes, such as the Payroll or Gross Receipts Tax. However, we assume that unregistered businesses are less likely than average to owe such taxes, since, in order to have escaped the notice of the Tax Collector, the businesses are likely to be smaller. Because we cannot accurately estimate the amount of business taxes likely to be generated as a result of the activities of the Business Identification Unit, we recommend that revenue projections for budgetary purposes be based solely on Business Registration fees.)

REVENUE COLLECTION FROM NEWLY IDENTIFIED BUSINESSES

Current Practices

As described above, the Audit Unit of the Business Tax Division has assigned three auditors to devote a portion of their time to the identification of unregistered businesses. Their typical procedure is to develop a list of possible unregistered firms, by comparing a source such as the yellow pages or a business directory with accounts listed in the BTS database, and then mail letters to the firms requesting that they call the auditor. Among the firms that respond and are doing business for profit in San Francisco, most do not have sufficient payroll or gross receipts to owe business taxes. (This is consistent with overall statistics, which show that up to 90 percent of businesses are exempt from business taxes.)

Our interviews with auditors revealed that the tax exempt businesses that they identify are told that they must register with the City. However, there is no procedure in place for anyone in the Tax Collector's Office to follow up to ensure that such firms do, in fact, pay their registration fee and obtain a Business Registration Certificate. Auditors do not check on this themselves; nor do they provide a list of newly identified businesses that should register to anyone in the Investigations Division.

---

[6]The Tax Collector should track not only the number of previously unregistered businesses registered by the Business Identification Unit, but also the amount of Payroll and Gross Receipts Tax collected from these businesses. The position may be justified even if fewer than 590 businesses are identified per year, as long as total revenues collected from them by the Tax Collector exceed $75,000.

While registration of non-Payroll/Gross Receipts taxpaying businesses is allowed to slip through the cracks, those newly identified firms that are expected to owe such taxes are audited. Not surprisingly, such audits tend to yield higher deficiency billings than do audits of firms that have made regular tax payments. For this reason, auditors who identify unregistered businesses assume that they are entitled to audit these "finds" themselves: high deficiency billings redound to the credit of the individual auditor. This is one reason that the auditors with part-time responsibilities for identifying unregistered businesses do not pursue identification more aggressively. They are only interested in identifying as many businesses as they personally would have time to audit.

Recommended Practices

The Management Analyst coordinating the Business Identification Unit should be authorized to establish a BTS account for all newly identified unregistered businesses. These accounts should contain an identification code to enable ISD to generate special status reports on the Business Identification Program. Such businesses should be notified by mail or telephone that they have 30 days to register with the City. The Management Analyst should obtain a monthly report from ISD showing the registration status of all such accounts, and follow-up with those firms that fail to register.

The Management Analyst should briefly interview all newly identified unregistered businesses by telephone (or request information by mail) to determine whether or not they are likely to owe Payroll/Gross Receipts Tax. Those that may owe such tax should be required to complete tax statements for all of the years they have been in business in San Francisco.

Such statements should be reviewed by auditors, but the practice of conducting field audits of all newly identified firms with taxes due should be discontinued, because auditing should not be used purely as a collections technique, until less costly (i.e. time-consuming) methods of collections have been attempted. A small number of such accounts could be selected for field audit, if the desk review of their submitted statements indicates that the accounts are relatively large and complex, and the statements appear to be inaccurate. The remainder should be subject to the regular collections process, as outlined in Section IV.2.

SUMMARY

There is no unit of the Tax Collector's Office with clear responsibility for registering businesses. The Business Tax Division and the Investigations Division make limited attempts to identify businesses that need to register, but estimates of the number of unregistered firms doing business in San Francisco range from 9,000 to 53,000. Unregistered businesses cost the City an estimated maximum of $6.8 million annually in business registration fees and up to $81.3 million in Gross Receipts and Payroll Taxes.

The Tax Collector should establish a Business Identification Unit in the Business Tax Division, with responsibility for identifying and registering businesses. This Business Identification Unit should work with City Departments, the Chamber of Commerce and other branches of government to identify all businesses operating in San Francisco.

The Business Identification Unit should track all identified businesses to ensure that they actually register with the City. Those that may owe Payroll and Gross Receipts Taxes should be required to submit tax statements and payments. Only large, complex accounts with statements that appear to be inaccurate should be audited; the rest should be subject to the standard collection procedures recommended in Section IV.2.

RECOMMENDATIONS

The Tax Collector should:

1. Establish a Business Identification Unit under the Business Tax Section, and hire a Limited Tenure 1832 Management Analyst to coordinate the Unit;

2. With the Chief Auditor (manager of the Business Tax Division), establish performance measures and procedures for the Business Registration Unit, including a goal of registering at least 590 previously unregistered firms per year;

3. Direct the Business Identification Unit to use information from the Assessor's roles to identify businesses for registration;

4. Direct the Business Identification Unit to use information from the State Board of Equalization, via the Controller's Office, to identify businesses for registration;

5. Maintain contact with the IRS to enter into an agreement whereby that agency provides information regarding businesses in San Francisco.

6. Direct the Business Identification Unit to develop a tracking system to permit follow-up with businesses that fail to register, and to permit tracking of Business Registration Fees and business taxes collected as a result of identification efforts.

7. Direct the Business Identification Unit to transfer all accounts for which registration and tax statements, with payment, are not immediately forthcoming to the Accounting Division, which should initiate standard collection notifications (as outlined in Section IV.2) and, if necessary, refer the account to the Collections Division.

8. Direct the Audit Unit to conduct desk reviews of business Payroll and Gross Receipts Tax statements, and to select only a limited number of such accounts for audit, based on the size and complexity of the account, and the appearance of inaccuracy in the statements.

9. Report to the Board of Supervisors annually about the accomplishments of the Business Identification Unit, including the number of businesses identified and registered, total revenues from registration and total revenues from business taxes collected from such businesses.

The Board of Supervisors should:

10. Approve legislation prohibiting any City department from providing services to businesses that cannot show proof of Business Registration;

COSTS/BENEFITS

The annual cost of an 1832 Management Analyst to coordinate the proposed Business Identification Unit in the Business Tax Division would be $75,000, including salary and fringe benefits. We propose that this be a limited tenure position, to be eliminated if the Business Identification Unit fails to register at least 590 previously unregistered firms in any fiscal year (which would yield approximately $75,000 in annual registration fees alone), or to generate at least $75,000 in combined business registration fees and Payroll/Gross Receipts Tax payments from previously unregistered businesses. Additional annual revenues of approximately $1.2 million to $6.8 million from Business Registration fees and up to $81.3 million of additional annual tax revenues from Business Gross Receipts and Payroll Taxes may also be realized for the City's General Fund. Assuming that these unregistered businesses owe the average annual Gross Receipts and Payroll Taxes paid by businesses to the City, $81.3 million annually in such taxes would also be lost; however, it is likely that many unregistered businesses are smaller businesses, and therefore the amount of Gross Receipts and Payroll Taxes is likely to be lower than $81.3 million.

SECTION III.4: TAXICAB DRIVER STATUS

The Tax Collector has not determined whether taxicab drivers should be classified as employees or independent contractors for the purpose of paying the City's business taxes. As a result, taxicab companies are not including taxicab driver payroll costs and fare intake in calculating and paying business taxes owed to the City, nor are taxicab drivers paying business registration fees to the City.

The Tax Collector should establish a checklist for taxicab companies to determine whether drivers are employees or independent contractors. Depending on whether taxicab drivers are classified as independent contractors or as employees, we estimate that the Tax Collector would realize additional annual revenue of $702,750 to $1,376,700.

Taxicab drivers can either be categorized as independent contractors or as employees of individual taxicab companies. If they are classified as independent contractors, they must register with the Tax Collector and pay the City's annual business registration fee. If they are classified as employees, the taxicab company with which they are associated must pay the City's annual business registration fee and calculate the amount of annual San Francisco business taxes owed. The amount of taxes owed would be based on the taxicab driver salary and benefit costs as part of payroll tax or drivers' fare intake as part of the gross receipts, whichever is greater.

The Tax Collector has not provided guidelines regarding the classification of taxicab drivers. As a result, taxicab companies do not include taxicab drivers' receipts (i.e., receipts are not included in calculating gross receipts) or payroll costs in calculating businesses taxes owed, and taxicab drivers never register as independent contractor businesses. Therefore, the City receives no business tax revenues from this source.

The License Section currently administers 4,685 Police Department taxicab driver licenses.[1] The Police Department reports that there are currently 36 taxicab companies in San Francisco, for an average of 130 cab drivers per company. Based on an average annual salary of $20,000,[2] if all taxicab drivers are classified as independent contractors, the Tax Collector loses $702,750 annually.[3] If all taxicab drivers are classified as employees, the Tax Collector loses an estimated $1,376,700 annually.[4]

The classification of taxicab drivers would vary from company to company, based on the behavior and guidelines of the companies and drivers. In 1991, the 6th District Court of Appeals looked at a number of factors in deciding the status of taxicab drivers in Santa Cruz, California.[5] Using the key factors in the Santa Cruz transportation case, we established the following checklist for taxicab companies to use to determine whether they should classify their drivers as employees or independent contractors. The first two criteria are given a weight of two; the last two are given a weight of one. Companies should tally their total scores. If they receive a score of four or more, they should classify their drivers as employees. If they receive a score of less than four, they should classify their drivers as independent contractors.

---

[1]As noted in Section II.1 of our report, these licenses are renewable annually. Each license is issued to a single individual; the number of licenses administered is an indication of the total number of San Francisco taxicab drivers.

[2]According to the *American Almanac of Jobs and Salaries*, the 1991 median salary for taxicab drivers was $17,628. Based on average annual inflation of two percent, the 1995 median salary for taxicab drivers would be $19,463. We have inflated the salary 2.8 percent, because the total median salary in San Francisco is higher than average, according to the 1990 United States Census.

[3] $150 registration for businesses with gross receipts of $20,000 times 4,685, the number of licensed taxicab drivers.

[4] 1.5 percent payroll tax times $20,000 times 98 percent of the total 4,685 licensed taxicab drivers. At an average annual salary of $20,000, a company would need to employ at least nine persons to be liable for the payroll tax, given that companies owing $2,500 or less are exempt. According to the Police Department, approximately one-third (twelve) of the 36 taxicab companies in the City employ eight drivers or less; these twelve companies therefore employ a maximum of 96 licensed taxicab drivers. Therefore, taxicab companies would owe payroll taxes for the remaining 98 percent, or 4,589 taxicab drivers (of the total 4,685 licensed drivers).

[5]*Santa Cruz Transportation, Inc. v. Unemployment Insurance Appeals Board* (1991); which is also being used as the basis for the State Employment Development Department's (EDD) criteria.

Table 15

Checklist to Determine Employment Status of Taxicab Drivers

1. Do you have the right to terminate your drivers?

   If you answer yes, score "2"

2. Do you specify the behavior of your drivers (their shift, their breaks, their clothing, whether or not they accept credit, whether or not they are required to pick up customers based on dispatcher instructions)?

   If you answer yes, score "2"

3. Are your drivers required to provide a reckoning of fares, as opposed to renting the cab for a fixed fee and providing no information in regard to the use of the cab during that time?

   If you answer yes, score "1"

4. Do you, as opposed to your drivers, advertise your services, including placing your company's name on the taxicab?

   If you answer yes, score "1"

If your total score is equal to four or more, classify your drivers as employees. If your score is less than four, please notify your drivers that they must obtain a Business Registration Certificate from the Tax Collector's Office.

Whether or not the Tax Collector would have the authority to collect registration fees or business taxes retroactively, once a determination as to the status of the taxicab drivers has been made, is dependent on the specifics of the individual case, according to the City Attorney. If the City Attorney determines that the Tax Collector does have the authority to collect retroactively, whether or not such retroactive collection should be implemented would be a policy decision for the Treasurer and Tax Collector, since payment of back taxes or accumulated registration fees might pose a serious hardship for businesses or individuals. For example, a taxicab driver earning $20,000 may have difficulty paying a lump sum of five years' registration fees, at $750 ($150 annual fee x 5 years). If the Tax Collector decides to collect retroactive payments, additional one-time revenue of $3,513,750 to $6,883,500 for five years of retroactive payments could be collected.

SUMMARY

The Tax Collector has not provided guidelines regarding the classification of taxicab drivers. As a result, taxicab companies never include taxicab drivers' receipts as part of gross receipts or payroll costs in calculating businesses taxes owed, and taxicab drivers never register as independent contractor businesses. Therefore, the City does not receive any business tax revenues from this source.

RECOMMENDATIONS

The Tax Collector should:

1. Establish a checklist for determining the status of taxicab drivers as independent contractors versus employees, in conformance with the recommendations contained in this report, and immediately begin collecting these revenues.

The City Attorney should:

2. Determine whether the Tax Collector has the authority to collect retroactive registration fees and business taxes in this case.

The Board of Supervisors and the Tax Collector should:

3. Make a policy decision regarding the retroactive collection of registration fees and business taxes, if the City Attorney determines that the Tax Collector has the authority to collect retroactively in this case.

COSTS/BENEFITS

Additional annual revenue of an estimated $702,750 to $1,376,700 would result from providing guidelines to taxicab companies and drivers regarding the employment status of taxicab drivers. If the Tax Collector collects retroactive payments, additional one-time revenue of $3,513,750 to $6,883,500 for five years of retroactive payments could be collected.

SECTION IV.1: DELINQUENT COLLECTIONS PROCESS: BUSINESS TAX

Approximately 31 percent of San Francisco businesses (18,000 to 19,000 per year of an estimated total of 60,000) do not file a Business Tax Registration Statement with the Tax Collector as required. For those businesses, the Tax Collector inflates the estimated outstanding Business and Payroll Tax in statements mailed to delinquent businesses to encourage taxpayers to respond. As a result, taxpayers are confused and the Tax Collector's customer service staff resources are overburdened. Also, the Tax Collector does not maintain records of taxpayer response, so that he cannot evaluate the efficacy of the overstated estimates. Finally, the Tax Collector uses these inflated calculations to estimate outstanding revenue, thereby overstating receivables.

In addition, the Tax Collector does not impose penalties against businesses for each delinquent action, which resulted in estimated lost revenues to the City of $1.8 to $1.9 million in 1994. We recommend that this penalty be imposed for each delinquent action. Implementation of this recommendation should result in estimated increased revenues to the City of $939,800 annually.

The Business Tax Division also does not forward delinquent business tax accounts to the Investigations Division until over one year after the accounts become delinquent. Follow-up on such delinquent business tax accounts should be conducted by the Accounting and Collections Divisions within 60 days. More reasonable estimates of delinquent business taxes owed, including penalties, and expediting notices to delinquent taxpayers could eliminate these problems and encourage taxpayer compliance.

This section of our report analyzes the Tax Collector's activities when a business does not file a Business Tax Statement with the Tax Collector's Office. We reviewed the Tax Collector's method of estimating overdue taxes, incentives for delinquent businesses to submit their Statements, the Tax Collector's method for estimating outstanding revenue, penalties, and the speed of collections.

We found that the Tax Collector:

- overstates the amount of outstanding taxes, which results in customer complaints and a consequent drain of Tax Collector resources;
- has not tracked taxpayer response to the overdue statements to determine whether using inflated amounts provides an incentive for taxpayers to respond quickly;
- uses the overstated, unrealistic estimates as a basis for estimating outstanding revenue;
- does not forward the delinquent accounts to the Investigations Division for collection until over one year after they become delinquent, even though sooner collection efforts are most likely to be effective.

We also found that almost one-third of all registered businesses do not file their annual Business Tax Statements (18,000 to 19,000 of a total of 60,000 registered businesses).

We recommend that the Tax Collector estimate outstanding taxes realistically; that the Tax Collector use realistic overdue tax amounts in estimating total outstanding revenue; that the Tax Collector impose an initial $500, and subsequent $100 penalties against businesses for each failure to file, failure to provide financial information or failure to register within a given year; and that delinquent accounts be forwarded to the proposed Accounting and Collections Divisions immediately to improve collection efforts. Implementation of these recommendations could result in increased revenue of approximately $1 million per year, fewer businesses failing to file their taxes, improved taxpayer services, improved recordkeeping and improved additional collections of overdue revenue.

In order to obtain maximum benefit from the recommendations made in this Section, the Tax Collector should streamline and prioritize overall collections efforts. We address this broader set of issues in Section IV.2 of this report.

This Section of our report is organized as follows:

- Estimated Overdue Tax Bills (known as Notices of Determination), including:
  - √ Background;
  - √ Method of Calculation, Taxpayer Response, and Recommended Alternative Method of Calculation (including incentive penalties), and
  - √ Success of Inflated Estimates as an Incentive to Respond;
- Penalties; and
- Collections, including:
  - √ Scheduling; and
  - √ Success of Collections Activities.

TAX COLLECTOR'S METHOD OF ESTIMATING AMOUNTS DUE FOR BUSINESSES FAILING TO FILE TAX RETURNS

Background

Every business operating in San Francisco must submit an annual Business (Gross Receipts) and Payroll Tax Statement, together with the calculated payment, to the Tax Collector's Office by the last day of February each year, even if the calculated payment is $0.

If a business does not submit an annual Business and Payroll Tax Statement, the Business Tax Division of the Tax Collector's Office sends that business an estimate of the amount of tax owed. This estimate is called a "Gross Receipts/Payroll Expense - Notice of Determination." Notices of Determination are sent in mid-June, or approximately three and a half months after the annual tax statements are due.

The Tax Collector's Office sends approximately 18,000 to 19,000 of these Notices of Determination each year. There are currently approximately 60,000 registered businesses in San Francisco. In other words, approximately 31 percent or nearly <u>one-third</u> of registered San Francisco businesses <u>do not file</u> a Business Tax Statement. In June, 1994, the Tax Collector's Office sent out 18,866 Notices of Determination valued at $144,256,939. This $144 million value represents 92 percent of the total $156 million of Gross Receipts and Payroll Tax revenues that were actually collected in FY 1993-94.

The Tax Collector's method for calculating the Notices of Determination overstates the amount of taxes owed by businesses, because the Tax Collector bases these estimates on an inflated percentage, rather than on a more reasonable estimate that would take into account such factors as past growth, business location, and type of business. The following paragraphs indicate the Tax Collector's method of calculating the Notices of Determination, taxpayer response to these Notices, the Tax Collector's use of the notices, and provide recommendations for modifying the calculation and use of the Notices of Determination.

Method of Calculation and Taxpayer Response

Method of Calculation

The Tax Collector's Business Tax Division calculates the amount a business owes based on 150 percent of the amount owed in the prior year. For example, if a business owed $5,000 in business taxes for 1992 and did not file an annual tax statement for 1993, the Tax Collector's Office would mail that business a Notice of Determination for payment of $7,500 for 1993. In addition, the Notice of Determination would assess additional costs for penalties of ten percent (i.e., $750 in the above example) and interest expenses at the rate of one percent per month (i.e., $305 for four months in the above example), for a total of $8,555.

Businesses that owe less than $2,500 are exempt from paying the City's Business and Payroll Tax. If a business had filed a tax statement for the previous year indicating that they were exempt, and that business does not submit the required annual tax statements for the current year, the Tax Collector's computerized system estimates the amount of tax owed to be $1 more than the City's current exemption. The following chart indicates the effective time periods for the City's business tax exemptions, the amount of the exemption, and the amount the Tax Collector determines that a previously exempt business must pay when he issues a Notice of Determination.

Table 16

Amount and Date of Business and Payroll Tax Exemption and the Amount of the Notice of Determination for Businesses Previously Exempt from Paying the Business and Payroll Tax

Date	Business is Exempt from Tax if Its Liability Is/Was at or Below This Amount	Minimum Amount of Notice of Determination
Prior to 1/1/93	$2,500	$2,501
1/1/93-12/31/94	$1,000	$1,001
As of 1/1/95	$2,500	$2,501

Notices of Determination are calculated automatically by the Tax Collector's computer system. If a business has not filed for several years, the Tax Collector's computerized system takes the type of business, the location, the estimated size and other factors into account for calculating the Notice of Determination.

Taxpayer Response

Taxpayers do not understand and are alarmed by the inflated amounts included in the Notices of Determination. This results in a high volume of complaint calls, which the Tax Collector cannot accommodate due to the Office's limited resources.

The Principal Auditor responsible for the Business Tax information and service counter reports that, after the Notices of Determinations are issued, approximately 75 to 80 percent of the calls and inquiries from San Francisco taxpayers are regarding these Notices of Determination. (The Tax Collector's Business Taxpayer information and service counter at City Hall, which includes four clerical employees and one to two Auditors, does not keep any records concerning the number of inquiries or the type of questions asked by San Francisco taxpayers.) Also, in CY 1994, the Tax Collector's staff disconnected its newly installed automated voice mail system due to the inability of the staff to keep up with the volume of messages and to return the calls in a timely manner.

Recommended Alternative Method for Calculating Notices of Determination

As an alternative to the current method of calculation, we propose that the Tax Collector make a reasonable estimate of overdue taxes, which includes the type of business, the location, the estimated size and other factors. Our survey found that the City of Los Angeles estimates taxes based on similar size and types of businesses for those businesses that fail to file tax statements. The Tax Collector's existing system could accomplish such calculations. (As noted above, the system makes such a calculation if a business has not filed for several years.) Since February 1, 1995, when the Tax Collector's Amnesty Program ended, the penalty for not filing an annual Business and Payroll Tax Statement was increased from ten percent to 20 percent of the unpaid taxes and a new penalty of an additional 20 percent of the unpaid amount for those accounts past due for over 90 days were added as additional incentives for businesses to pay their taxes on a timely basis.

In cases where the estimated tax is below the Small Business Exemption, in accordance with an ordinance approved by the Board of Supervisors in October, 1994 (File 127-94-10), businesses that do not file their annual Tax Statements with the Tax Collector's Office will lose their tax exempt status for that year.[1] For example, if a business calculates its business tax liability to be $500, and files its Business Tax Statement on time, that business is exempt from paying the tax. If however, the same business does not submit its Business Tax Statement, and the Tax Collector calculates its business tax obligation at $500, the Tax Collector would notify the business: (1) that its calculated business tax obligation is $500; (2) that the business will be exempt from any obligation, if its calculated tax is less than

[1]The new ordinance will affect business tax liabilities accruing on or after January 1, 1995. The impact of this legislation will therefore not be known until businesses file their 1995 Business Tax Statements, which are not due until the end of February, 1996. Although this amendment should encourage more businesses to file their annual Tax Statements, this provision will not materially affect those businesses that currently owe San Francisco Business Taxes.

$1,000 and the business responds within 30 days; and (3) if the business does not respond within 30 days, the tax exemption will be suspended for that tax year, and the business will owe $500, or whatever the calculated amount of business taxes.

The advantages of this proposed methodology are as follows:

(1) *Customer Satisfaction*
Taxpayers are more likely to understand a Notice of Determination that includes a reasonable tax estimate, along with a substantial penalty for failure to respond, instead of a Notice that includes an inflated tax estimate that is not based on any financial data. In addition to an intrinsic customer service improvement, enhanced taxpayer understanding would reduce the Tax Collector's workload, since taxpayers would not call the Tax Collector to complain or request clarification.

(2) *Improved Incentives to Respond*
The recently approved 20 percent penalty (plus an additional 20 percent after 90 days) for unpaid taxes is likely to be more collectable. A taxpayer could easily protest an artificially inflated tax obligation, however, the Tax Collector has the right to impose the increased penalties based on the amount owed that remains unpaid or underpaid. In addition, because the Notice of Determination would be more readily understandable, businesses would understand their obligation to respond quickly or risk substantial penalties.

(3) *Improved Outstanding Revenue Estimates*
This method of calculating Notices of Determination would differentiate between the realistic estimate of outstanding taxes and the penalties. The Tax Collector could use the base outstanding tax amount to estimate actual outstanding revenue owed to the City. Assessed penalty revenue could be recorded separately, and the projected revenue from such penalties could also be maintained separately.

Success of the Inflated Overdue Estimates as an Incentive to Respond

The Tax Collector has maintained no records indicating the success of the inflated Notices of Determination as an incentive to file the Business Tax Statement; that is, the Tax Collector does not track revenues collected as a result of these Notices of Determination. Because of the Tax Collector's failure to maintain these kinds of records, the success of the Department's activities in collecting business tax revenues from the Notices of Determinations cannot be determined at this time.

Types of records that the Tax Collector should maintain include the reason the taxpayer remits payment (e.g., is the taxpayer responding to a regular invoice, a Notice of Determination, a written, telephone, or in-person contact from an Investigator, etc.) elapsed time between Tax Collector contact and taxpayer response, whether or not the taxpayer disputes a determination by the Tax Collector, and whether or not the taxpayer remits payment in full, remits partial payment and negotiates a payment plan, or does not remit payment. Performance

measures that would indicate the efficacy of the Notices of Determination might include average response time after Notices are mailed (i.e., telephone calls), average time lapse between the Tax Collector's mailing the Notice of Determination and the business mailing the Business Tax Statement, and percent of businesses that respond within 30 days, between 30 and 90 days, after 90 days, or not at all.

Based on these records and performance measures, the Tax Collector could make an informed decision regarding future collection strategies to enhance and maximize the efforts of the Tax Collector's Office.

PENALTIES

The Tax Collector has not used his authority to impose a separate penalty against businesses that simply fail to file their tax returns. As a result, substantial revenue is lost.

According to the City's Administrative Code, in 1994, the Tax Collector could impose a penalty of $100 for each year a business failed to do any of the following: (1) file a tax return, (2) provide financial information upon request, or (3) register as a business.[2] This $100 penalty was in addition to any other liability or penalty that was imposed. After the Amnesty Program, which ended January 31, 1995, this failure to file penalty fee was increased to $500.

The Tax Collector has established a policy of imposing a penalty <u>only once per year</u> against any given business. As a result, the Budget Analyst found that only 70 of the total 18,866 Notices, or less than 0.4 percent of the delinquent Notices issued, included the $100 assessed penalty fee. Therefore, a total of only $7,000 of penalty fees was assessed during 1994, or $1,879,600 less than the amount of penalty revenue that could have been assessed. If a comparable 18,866 Notices of Determination are issued in 1995, this would result in $9,433,000 of penalty assessments, based on the current $500 penalty rate, which is not currently being assessed or collected. Although $500 per occurrence may be too great a penalty for many businesses to incur, the Tax Collector should impose a penalty per occurrence rather than only once per year. An initial penalty of $500, with subsequent occurrences during the same year resulting in an additional $100 would be reasonable. If approximately the same number of Notices of Determination were issued, and the Tax Collector was able to collect approximately 50 percent of the assessed $100 additional penalties, the Tax Collector would receive approximately an additional $939,800 of revenues per year.

Imposing such a penalty would serve as an incentive for future compliance, since businesses filing a Business Tax Statement on time would not be required to pay the $500 or subsequent $100 penalties. The possibility of being penalized also provides an incentive for businesses to provide timely financial information to the Tax Collector and to comply with the City's Business Registration Certificate procedures. Failing to assess the penalty for each of these occurrences eliminates such incentives.

---

[2]According to San Francisco's Municipal Code, Part III, Article 12-B, Section 1009.2.

Although the Tax Collector provided the Budget Analyst with a memorandum dated September 3, 1991 from the then Acting Chief Auditor, explaining the Tax Collector's position on this matter, in the professional judgment of the Budget Analyst, this policy provides an incentive for businesses to continue their delinquent practices throughout the year, without imposition of any additional penalties. The City Attorney's Office was unable to provide a clear interpretation of the existing Municipal Code to indicate whether the Tax Collector has the authority to assess such penalties more than once per year. We therefore recommend that Part III, Article 12-B, Section 1009.2 of the City's Municipal Code be rewritten to clearly indicate that a penalty will be assessed for each incidence of violation of this provision.

COLLECTIONS

Scheduling

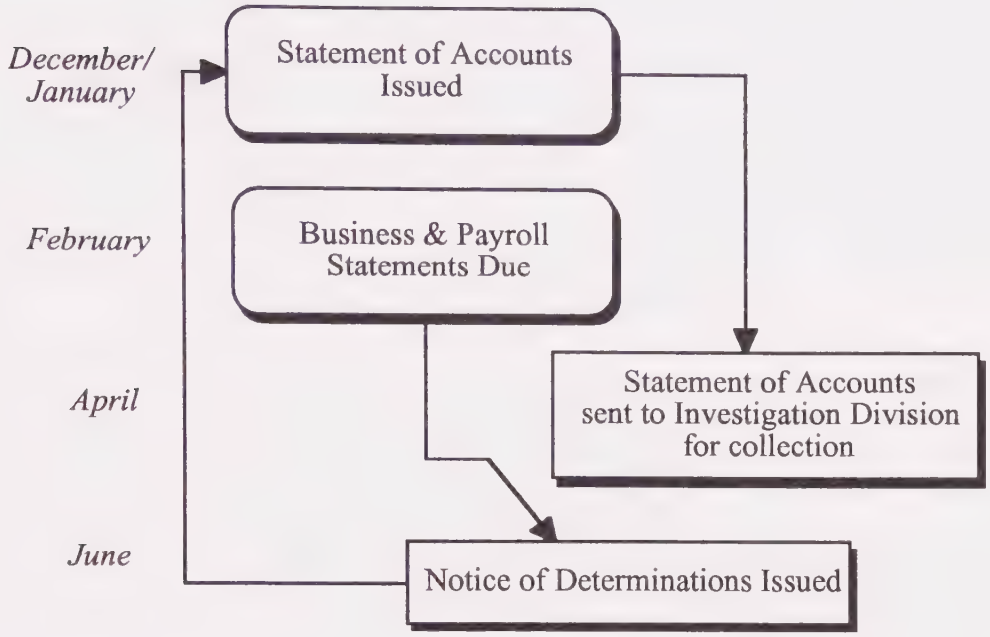
The Tax Collector's current schedule for pursuing businesses delinquent in paying their Business and Payroll Taxes can often postpone the beginning of collection procedures until over a year after the tax is due. This delay substantially reduces the Tax Collector's ability to collect this delinquent revenue. The following paragraphs outline the Tax Collector's current procedures for beginning collection procedures against businesses delinquent in paying their taxes, and provides recommendations for streamlining the current schedule.

As discussed above, businesses are responsible for filing and paying their annual Business and Payroll Tax Statements by the end of February following the tax year. If the Tax Collector does not receive this information, a Notice of Determination is sent to the business in June, or approximately four months after the Business Tax Statement and payments were due.

At the same time, the Business Tax Division maintains a Statement of Accounts for each business that reflects the delinquent business taxes owed to the City, including Gross Receipts Taxes, Payroll Taxes, Hotel Taxes, Parking Taxes Business Registration Certificate fees and audit deficiencies. These Statement of Accounts are sent to the taxpayer approximately once a year. In 1994, the Statement of Accounts were issued in January. (The Tax Collector reissued the statements in December, 1994 to include updated information regarding the Amnesty Program.) The Statement of Accounts information is then forwarded to the Investigations Division, for collection on these delinquent accounts, after approximately another three to four months. In 1994, the Statement of Accounts data was forwarded to the Investigations Division in April. The following flow chart reflects this current schedule.

Chart 8

Current Schedule for Issuing Statements of Accounts and Beginning Collection Procedures



Given the current schedule, the delinquent taxpayer receives a Notice of Determination in June, and then does not receive another delinquent notice until the Statement of Accounts the following December or January, approximately six or seven months later. This delinquent Business and Payroll Tax information is not forwarded to the Investigations Division until the following April, or one year and two months after the account becomes delinquent.

Unless one of these delinquent accounts is selected to be audited (as discussed in Section III.1 of this report), the delinquent business may never receive another letter, telephone call or visit regarding this delinquent Business Tax owed to the City of San Francisco for another year. Studies have shown and the City's Tax Collector agrees that the more time that elapses, the lower the likelihood there is to collect on these delinquent accounts. In fact, the U.S. General Accounting Office recently conducted a nationwide survey on State's delinquent tax collection methods and found that the average amount of time spent trying to actively collect delinquent taxes before an individual case is removed from active collection status is 12 months.[3] However, in San Francisco, these delinquent accounts are not even referred for collection efforts until over 14 months after the account becomes delinquent. Such delay in forwarding accounts to the Investigations Division

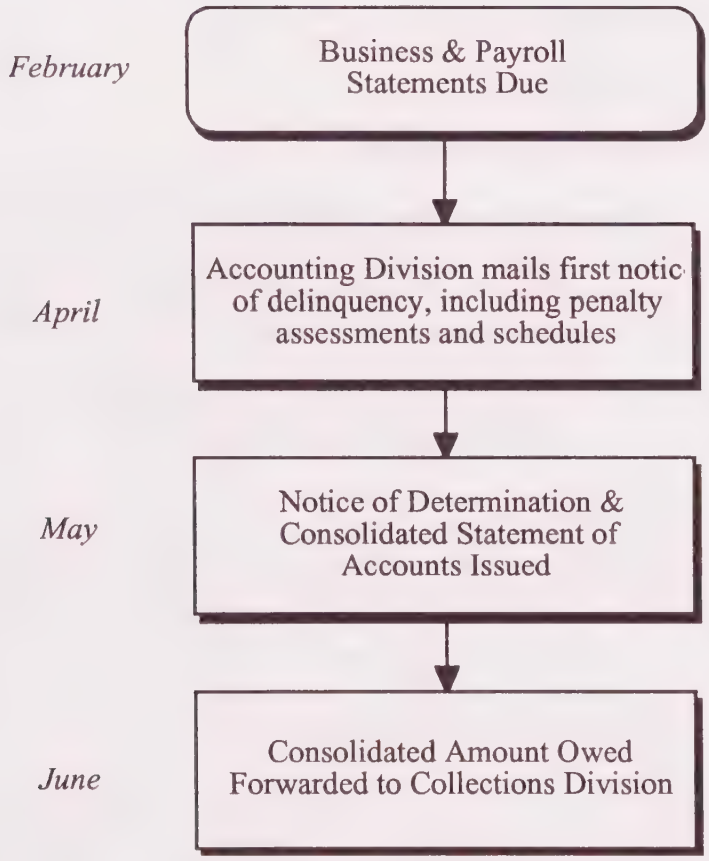
[3]United States General Accounting Office, Tax Administration: State Tax Administrators' Views on Delinquent Tax Collection Methods. Fact Sheet for the Chairman, Subcommittee on Oversight.

substantially reduces the Tax Collector's ability to collect delinquent Business Tax accounts, although the amount of such loss is difficult to calculate.

The Budget Analyst recommends that the Tax Collector's Office implement a more streamlined and effective approach to collect delinquent Business Taxes, as shown on the following page.

Chart 9

Proposed Schedule for Issuing Statements of Accounts and Beginning Collection Procedures



As reflected above, the Business and Payroll Statements and payments could continue to be due by the end of February each year. However, if the statements and payments are not received, the proposed Accounting Division (See Section I.1 of this report) would mail out the first delinquency notice in April, which would include another Business and Payroll Tax Statement, identifying any penalties owed and the additional penalties that will accrue if the taxpayer does not immediately complete the enclosed Tax Statement and remit any assessed amounts owed. If no response is received, in May, the Accounting Division would then calculate a realistic Notice of Determination, based on the estimated amount of taxes owed according to the type of business, the location of the business and the estimated size of the business, together with a consolidated Statement of Account, which would reflect any previous itemized amounts owed to the City. If a response is not received

within another 30 days, the account should then be forwarded to the Collections Division to begin active collection efforts (See Section IV.2 concerning the Consolidated Collections Process).

Although the Tax Collector indicates that it currently takes several months to input the Business and Payroll Statement data, such that delinquent notices cannot be issued for at least three to four months, the planned addition of scanner equipment should expedite this process (see Section I.1). Under the proposed process, the Accounting Division would be responsible for the initial notifications of these delinquent taxpayers. In this way, active collection efforts against delinquent taxpayers could begin within a maximum of 30 to 60 days after the tax was due. Also, the Tax Collector could, as an interim measure, note receipt of a tax return in a suspense file without entering all of the information on the return. For businesses that have not filed, he could then notify non-filers that they are delinquent in filing, without estimating the amount such non-filers owe.

SUMMARY

Approximately 31 percent, or almost one-third of San Francisco businesses (18,000 to 19,000 per year of an estimated total of 60,000 businesses) do not file a Business Tax Statement with the Tax Collector's Office as required. For those businesses, the Tax Collector inflates the estimated outstanding Business and Payroll Tax in statements mailed to delinquent businesses, does not maintain records of taxpayer response, and uses these inflated estimates to estimate outstanding revenue. As a result, taxpayers are confused and alarmed, the Tax Collector's customer service staff resources are overtaxed, and the Tax Collector cannot evaluate the efficacy of the overstated estimates.

The Tax Collector did not impose a $100 penalty against businesses for failing to file a Business Tax Statement, which resulted in lost revenue of $1.8 to $1.9 million in 1994. Based on the Tax Collector's current policy, the current $500 penalty would not be imposed for each violation incident. We recommend that a penalty fee, of possibly $100 for each subsequent occurrence within a given year, be imposed for each delinquent filing.

The Business Tax Division may not forward delinquent business tax accounts to the Investigations Division for over a year and the Investigations Division makes these accounts its lowest priority. As a result, collections are not maximized. Delinquent business tax accounts should be forwarded to the Accounting and Collections Divisions for follow-up within 60 days. More reasonable estimates of delinquent business taxes owed, plus imposing penalties, and expediting notices to delinquent taxpayers would eliminate these problems and encourage taxpayer compliance.

In order to obtain maximum benefit from the recommendations made in this Section, the Tax Collector should streamline and prioritize overall collections efforts. We address this broader set of issues in Section IV.2.

RECOMMENDATIONS

The Tax Collector should:

1. Calculate the amount of unpaid Gross Receipts and Payroll Taxes based on the type of business, the location, the estimated size and other relevant factors for purposes of the Notice of Determination;

2. Implement a more streamlined and effective schedule to collect delinquent Business Taxes immediately, such as is described in the above section;

3. Impose a penalty for each violation of Part III, Article 12-B, Section 1009.2 of the Municipal Code.

The Board of Supervisors should:

4. Amend Part III, Article 12-B, Section 1009.2 of the City's Municipal Code to indicate clearly that a penalty will be assessed for each incidence of violation of this provision.

COSTS/BENEFITS

Charging a $100 penalty against taxpayers for each subsequent violation of the City's Code would result in increased revenue of approximately $939,800 annually. In addition, using a realistic estimate for assessing unpaid business taxes, including penalties and expediting the delinquent collection's process should reduce taxpayer frustration, improve the taxpayer's incentives to respond, reduce the business tax delinquency rates and therefore increase overall revenues for the City.

SECTION IV.2: CONSOLIDATED COLLECTIONS PROCESS

The Tax Collector's methods of collecting delinquent revenue do not result in the highest possible revenue return. For example, collections personnel in certain instances collect on only one type of delinquent revenue from a business, when that business owes more than one type of delinquent tax. Also, the Tax Collector has not established a multi-variable, automated prioritization system for all delinquent accounts to ensure that collections personnel pursue accounts with the highest possible return. The Tax Collector uses labor-intensive collections methods, such as in-person visits, but does not perform simple, routine collections activities such as mailing delinquency notices.

The Tax Collector should: combine the Investigations Division, the Bureau of Delinquent Revenue, and the Legal Division into a single Collections Division; should implement the non-labor intensive, effective collections techniques of mailing consolidated bills and seizing checking accounts; and should expand the use of the newly acquired Columbia Ultimate Business System (CUBS) to establish a prioritization system for pursuing all delinquent accounts.

Implementation of these recommendations will result in additional annual revenue of up to $150,000 to $1.5 million.

One of the primary functions of the Tax Collector's Office is to collect delinquent revenue. As part of this management audit, we identified the Tax Collector's activities related to the collection of delinquent revenue, and considered whether the Tax Collector could collect delinquent revenue more effectively.

To conduct this analysis, we interviewed various staff members within the divisions responsible for delinquent revenue collection, accompanied Investigations Officers in the field as they collected delinquent unsecured personal property (UPP) taxes, analyzed our survey results, reviewed existing documentation, including the General Accounting Office (GAO) study, State and local codes, and various publications, and reviewed the Tax Collector's collection records.

We found that costs would be reduced, revenues increased, and customer service improved, if the activities of the Legal Division, the Investigations Division and the Bureau of Delinquent Revenue were consolidated into a single Collections Division. Similar benefits would result from the establishment of a system for prioritizing collection activities, and from implementing non-labor intensive, routine collections activities.

This section of our report does the following:

- Describes the Tax Collector's current activities and organization in regard to delinquent revenue collection;
- Identifies inefficiencies with the current organization, including collection priorities, resource allocation, collections methods, account information, scheduling, and delinquent revenue collection activities;
- Delineates an ideal reorganization of delinquent revenue collection activities; and
- Discusses the practical implementation of this idealized reorganization.

THE WAY IT IS NOW

Three of the eight divisions of the Tax Collector's Office currently have responsibility only for pursuing delinquent revenues: the Legal Division, the Bureau of Delinquent Revenue, and the Investigations Division. In addition, the Business Tax Division and the Property Tax Division have responsibility for some activities related to pursuing delinquent revenues. The following paragraphs describe the functions of these five divisions as they relate to delinquent revenue collections.

Bureau of Delinquent Revenue

The purpose of the Bureau of Delinquent Revenue (BDR) is to centralize, investigate, enforce and collect delinquent accounts for user departments. Delinquent hospital bills represent the lion's share of BDR accounts, although the Municipal Code requires all City departments (except for the Port Authority, the Airport, the Public Utilities Commission, and the Department of Social Services) to refer accounts delinquent for 90 days to the Tax Collector. BDR's regular collections activities include telephone and by-mail pursuit. In addition, BDR currently seizes a delinquent accountholder's financial assets, such as checking accounts and wages, for delinquent medical bills. Seizing financial assets is accomplished by researching checking accounts, employers, and other information, preparing a Writ of Execution, and providing this Writ of Execution to the Sheriff's Department. The Sheriff's Department uses the Writ of Execution to seize the accountholder's assets from banks, employers, and any other relevant party.

BDR contracts with a collection agency for delinquent accounts of up to $2,500, as indicated in Section 1039-1 of the Municipal Code. To transfer larger delinquent accounts to a collection agency, the Tax Collector must obtain separate authorization from the Board of Supervisors.

Besides collecting delinquent departmental accounts, BDR researches and collects unpaid fees and taxes by submitting small claims during escrow and bankruptcy proceedings.

To perform its responsibilities, BDR is organized into two units: Delinquent Accounts, and Escrow and Bankruptcy. The Division has a total of 19 authorized positions, of which 18 are filled, including a Division Manager. The Division's FY 1994-95 budget is $1,672,179. In FY 1993-94, BDR collected $9,280,411 in delinquent revenues, including revenues paid directly to San Francisco General Hospital and Laguna Honda Hospital as a result of BDR activities.

Investigations Division

The Tax Collector's Investigation Division is responsible for the investigation of delinquent tax revenues referred by the Tax Collector's Property Tax, Business Tax and License Divisions and provides support services to the Tax Collector's Legal Division. The Division focuses on the collection of delinquent Unsecured Personal Property as its first priority, and other delinquent business taxes (i.e., Payroll/Gross Receipts, Hotel, Parking, etc.) as its second priority. The Division provides limited collections services to the Legal Division, BDR, and the License Division.

The Investigations Division also has a five-person Clearance Unit, including three Collection Officers and one Clerk Typist. This Unit researches all businesses submitting a Business Registration fee to determine whether these businesses have any outstanding accounts owed to the Tax Collector. If there are no outstanding taxes or fees owed, the Clearance Unit sends the firm a Business Registration Certificate. If there are delinquent taxes or fees, the Clearance Unit sends a letter indicating the amounts outstanding, and indicating that a Business Registration Certificate will not be forwarded until all accounts are paid in full. (This letter is the only point in the Tax Collector's entire operations at which a taxpayer might receive a comprehensive statement, including all outstanding balances.) In FY 1993-94, the Clearance Unit collected approximately $2 million.

The Investigations Division has a total of 20 authorized positions, of which 18 are filled, including a Division Manager. The Division's FY 1994-95 budget is $1,323,629. The following table indicates the Division's FY 1994-95 revenue by type.

Table 17

Investigations Division
CY 1993 Delinquent Revenue Collections by Type

Revenue Type	Amount
Regular U.P.P.	$6,033,303
Supplemental U.P.P.	3,601
Business Tax	1,103,247
Licenses	91,068
Small Claims Court	13,277
Bounced Check Collection	23,904
Real Estate	12,634
Hotel Tax	245,036
Parking Tax	22,519
Miscellaneous	1,847
Total	$7,550,436

The Investigations Division's primary collection technique is in-person visits to delinquent accountholders. In addition to in-person collections, the Investigations Division places liens on property for U.P.P. accounts over $20. Finally, the Investigations Division implements seizure and sale procedures for boats, in accordance with the State's Revenue and Taxation Code. According to the State Revenue and Taxation Code, the Tax Collector is empowered to seize any property, including financial assets, such as checking accounts, to recover delinquent UPP taxes. However, the Investigations Division does not seize checking accounts. In order to implement seizure proceedings for delinquent business taxes, the Tax Collector would require authorization from the Board of Supervisors.

Legal Division

The Legal Division's primary function is the collection of delinquent revenue claims. Most delinquent accounts referred to the Legal Division are business tax deficiencies; however, the Legal Division spends most of its time collecting delinquent medical treatment accounts.

The Legal Division has a total of five authorized positions, including two attorneys, two paralegals, and one clerk, all of which are filled. The Division's FY 1994-95 budget is $321,384. In FY 1992-93, the Division collected $4,675,000 in delinquent hospital bills and business taxes.

Business Tax Division

The Business Tax Division receives and processes the annual Business (Gross Receipts) and Payroll Tax Statements, together with the calculated payments submitted by every business operating in San Francisco each year.

If a business does not submit an annual Business and Payroll Tax Statement, the Business Tax Division sends that business an estimate of the amount of tax owed. This estimate is called a "Gross Receipts/Payroll Expense - Notice of Determination." Notices of Determination are sent in mid-June, or approximately three and a half months after the annual tax statements are due.

The Tax Collector's Office sends approximately 18,000 to 19,000 of these Notices of Determination each year. There are currently approximately 60,000 businesses in San Francisco. In other words, nearly one-third of registered San Francisco businesses do not file a Business Tax Statement (See Section IV.1 of this report for additional information on this process).

The Business Tax Division also maintains a Statement of Accounts for each business reflecting the delinquent business taxes, including Gross Receipts Taxes, Payroll Taxes, Business Registration Certificate fees, Hotel Taxes, Parking Taxes, other business taxes and audit deficiencies. These Statement of Accounts are sent to the taxpayer approximately once a year. The Statement of Accounts information is forwarded to the Investigations Division for collection after three to four months.

The Audit Unit of the Business Tax Division handles the initial collection of audited deficiency billings. Such billings are supposed to be referred to the Investigations Division if payment is not made within three to six months. However, the Budget Analyst found audited accounts that were not forwarded to the Investigations Division for more than one year.

Property Tax Division

The Property Tax Division collects payment for secured and unsecured property taxes and special assessments. It is easier to ensure payment of property taxes than other types of outstanding revenue, because the value of the real property typically exceeds the amount of the tax, and the real property is in a permanent, fixed location. If an individual is delinquent in paying his/her real property tax bill, the Recorder records a lien against the property automatically through the Controller's ISD. When ownership of the property is transferred, the Tax Collector collects the delinquent revenue. If the taxpayer continues to be delinquent in paying property tax for a period of five or more years, the Tax Collector seizes and sells the property at auction to collect the delinquent taxes. The process of collecting delinquent secured property taxes does not involve collections personnel in the Investigations Division or BDR. The Property Tax Division administers the tax default sale process and auctioning real property to recover delinquent property taxes. The Property Tax Division collects almost 100 percent of real property taxes over the long term. In FY 1993-94, the Division collected a total of $592,098,918 in non-delinquent secured

property taxes, including the regular and supplemental rolls, and $23,659,235 in delinquent secured property taxes.

The Property Tax Division is also responsible for billing and collecting non-delinquent Unsecured Personal Property taxes, which consist of approximately 90 percent accounts held by businesses and ten percent accounts held by individuals. In FY 1993-94, the Division collected $60,974,750 in total UPP taxes (including regular and supplemental) and $5,214,550 in delinquent UPP taxes. Delinquent UPP taxes are referred to the Investigations Division for collection.

FINDINGS AND INEFFICIENCIES

We identified inefficiencies in the Tax Collector's Office's collection of delinquent revenues. These inefficiencies are detailed in the following paragraphs.

Collection Priorities

The prioritization systems established by the different divisions of the Tax Collector's Office do not necessarily ensure that the maximum amount of revenues are collected using existing resources. For example, as noted above, the Investigations Division has established the collection of delinquent UPP taxes as its first priority: seven of the Division's nine Investigators, plus one Senior Investigator, are Field Investigators in charge of primarily collecting UPP Tax.

The Investigations Division manager has established UPP tax collection as a high priority for two reasons. First, delinquent UPP taxes may not be collected by an outside contractor (i.e., a collection agency) and the Legal Division does not pursue UPP delinquencies. Thus, if the Investigations Division does not pursue these delinquent UPP taxes, such revenues are foregone. Second, the Division is successful in collecting delinquent UPP taxes. However, the Tax Collector should develop a more sophisticated system for determining what accounts should receive collections priority, taking into account the fact that collections activities encourage voluntary compliance in the long run. Neglect of major categories of delinquent taxpayers in collections activities provides a strong incentive for such taxpayers to withhold future tax payments.

Underpaid outstanding delinquent revenue for business registration, payroll and gross receipts taxes, and hotel and parking taxes as of February 14, 1995, was $29,505,591[1]. The Investigations Division reported total collections on such delinquent business accounts of $2,078,228 during the previous year (1994). The Legal Division collected another $266,228 of such unaudited business taxes during 1994[2]. If the Tax Collector began 1994 with approximately the same amount of outstanding revenue for the various business taxes, the collection rate on such taxes

[1] This amount does not include outstanding tax balances estimated for the Notices of Determination by the Tax Collector's Office because businesses failed to file tax statements or the related interest and penalties on such balances.

[2] The Legal Division's total collections, excluding bankruptcies in 1994 was $1,064,913. Unaudited underpaid business taxes represented approximately 25 percent of these collections.

would have been only approximately 7.9 percent ($2,344,456 total revenue collected divided by $29,505,591 outstanding delinquent amount). This calculation only includes delinquencies for accounts that filed statements --- i.e., relatively collectable delinquencies. If accounts that failed to file statements at all were included, the outstanding amount would exceed $311 million and the collection rate on delinquent business accounts of the types listed above would be negligible. A larger portion of total outstanding revenue would likely be collected, if the Tax Collector implemented a prioritization system (see below).

The Legal Division has also established no written system to identify and pursue high priority accounts. As with the Investigations Division, accounts are prioritized according to category: trust fund accounts are considered first priority, business audit deficiency accounts are considered second priority, and mandatory duties to represent the Tax Collector, such as defending the City in foreclosures, are considered third priority. As a result, the Legal Division may spend time on a hard-to-collect, low-dollar-amount account, while the Statute of Limitations expires on collectible, valuable accounts.

The Bureau of Delinquent Revenue's prioritization system is the most formalized, and includes appropriate variables, i.e., statutes of limitations, amounts, and ease of collections. We recommend that these variables be used in establishing an overall prioritization system for delinquent accounts, below.

Resource Allocation

Establishing separate divisions for the collection of different types of revenue reduces the Tax Collector's flexibility, and may therefore result in lost revenue. For example, an influx of delinquent hospital bills could coincide with a diminution in delinquent UPP tax accounts, but, because collections personnel are separated into discreet divisions, resources cannot be moved from UPP tax collection to hospital bills.

Collections Methods

The Tax Collector has established no overall policies regarding preferred types of collection-related activities, and has not evaluated the efficiency of one activity over another. As a result, the various divisions of the Tax Collector's Office, and employees within the divisions, perform different types of collections activities, and staff may not spend their time as productively as possible.

For example, the Investigations Division Manager has established in-person delinquent tax collection as the preferred collection method. Field Investigators do not have the discretion to work in the office as opposed to in the field, even if a particular collection could be accomplished more effectively by telephone. (This practice of collecting in-person has been in place in the Tax Collector's Office for at least 14 years: the Budget Analyst's 1981 Review of the Operations of the Tax Collector's Office found that the Tax Collector's Investigators "spend an inordinate amount of time in the field making general inquiries, attempting to contact owners of businesses or properties and notifying taxpayers of delinquent accounts.")

According to a GAO survey of state tax collection agencies,[3] to which 43 of the 50 states responded, none of the states reported that in-person collections increase efficiency. Two-thirds (29 of the 43 states) had reviewed or were in the process of reviewing their use of field collection staff. Eight of these states had already limited or modified their revenue officers' roles to increase productivity and reduce travel costs by having field collectors employ telephone collection techniques.

Collections personnel do not perform their duties consistently. During this audit, we observed Investigations Division Field Investigators use of varying techniques to collect delinquent revenues, provide inconsistent responses to taxpayer questions, and fail to comply with the Investigations Division's policy that Investigators must review Business Registration Certificates at construction sites.

Lack of Accurate, Complete Account Information

Collections personnel do not have easy access to consolidated, consistent information that shows accurate total delinquent amounts due for businesses owing money. As a result, collections personnel may request only a portion of the total amount due from the businesses they visit. For example, a Field Investigator may make an in-person visit to a business to collect a delinquent UPP Tax, but neglect to collect other delinquent taxes or fees due from the same taxpayer.

During the course of this audit, we observed a Field Investigator visiting a business that owed $27,041 in delinquent Business and Payroll Tax and $10,664 in delinquent UPP Taxes.[4] The Investigator collected $500 as a partial payment toward the delinquent UPP Taxes, but was unaware of the outstanding amount of Business and Payroll Taxes. As noted above, the Investigations Division is responsible for collecting delinquent business and payroll taxes.

---

[3]"Tax Administration: State Tax Administrator's Views on Delinquent Tax Collection Methods, " General Accounting Office, February, 1994.

[4]At the same time, BDR had filed a claim against the business, which declared bankruptcy in 1989, to recover delinquencies of $49,185 incurred prior to the bankruptcy filing date. However, Investigations personnel cannot collect for debts incurred prior to a business declaring bankruptcy.

Furthermore, our investigation found that this same business had filed bankruptcy, thus stopping their payments on their delinquent UPP Tax bills for the period from 1989 through 1991. The delinquent bankruptcy account was estimated at approximately $49,185 and the Tax Collector's Office is currently receiving installment payments through bankruptcy court on this outstanding balance. As noted above, BDR is responsible for implementing collections against bankrupt businesses.

Automation

One reason that collections personnel do not collect for the entire amount due from an individual or business is that consolidated information showing the total amount due for all outstanding revenue types is difficult to obtain. Each Division refers to different or multiple databases. Also, although in some cases these databases can automatically calculate accrued interest and penalties, others cannot. Therefore, to determine the total amount due, an employee must look up a delinquent accountholder on more than one database, know which databases make automatic calculations, and personally calculate penalties and interest for those databases that do not perform these functions automatically. This research and calculation process is subject to human error, particularly since collections personnel are not necessarily skilled accountants.

In addition, a time lag can occur between the time the Cashier Division receives a payment and the time the relevant Division updates its database to reflect payment. Thus, the amount that appears in any given database as outstanding might overstate the actual amount due.

The Tax Collector has recognized the need for a consolidated delinquent tax statement, has obtained budgetary approval for the Columbia Ultimate Business System (CUBS), to be put into operation as of May 1, 1995, and has devoted personnel time to learning and operating CUBS. CUBS can be programmed to accept the various taxes downloaded from the Unsecured and Business Tax Systems, and to compute interest and penalties. However, CUBS cannot produce a consolidated delinquent tax statement until each taxpayer has only one account number. (See Section I.1 for information on consolidating accounting functions.)

Summary of Current Delinquent Revenue Collection Activities

The standard activities typically associated with collecting delinquent revenue are the same, regardless of the type of revenue being collected, with certain exceptions. Collections activities include mailing letters, making telephone calls, making in-person visits, filing small claims, seizing property, placing liens (to the extent that such liens are authorized by local and State legislation), referring accounts to collection agencies (with the exception of Unsecured Personal Property tax collection, which cannot be performed by a contractor), and suing or settling out of court.

The Investigations Division, BDR, and the Legal Division currently perform these activities separately, and collections activities are not standardized. For example, the Divisions do not automatically mail notices of delinquent accounts to debtors. Investigators may send letters, at their discretion. Form letters that would be updated to specify the taxpayer's identity and the total amount due have not been prepared; Investigators must create their own individual letters. In the Investigations Division, Investigators are expected to focus their efforts on in-person collections. In the Bureau of Delinquent Revenue, Investigators may pursue collections by letter, by telephone, or through small claims court according to the strengths and preferences of individual employees.

Not only are delinquent revenue collections activities inconsistent from Division to Division, the activities themselves are not necessarily the most efficient use of staff time. In-person collections require more resources than other collection methods, because in-person collections are labor-intensive, time-consuming, require automobile or other travel methods and, ideally, should rely on automated systems for tracking accounts from the Investigators in the field.

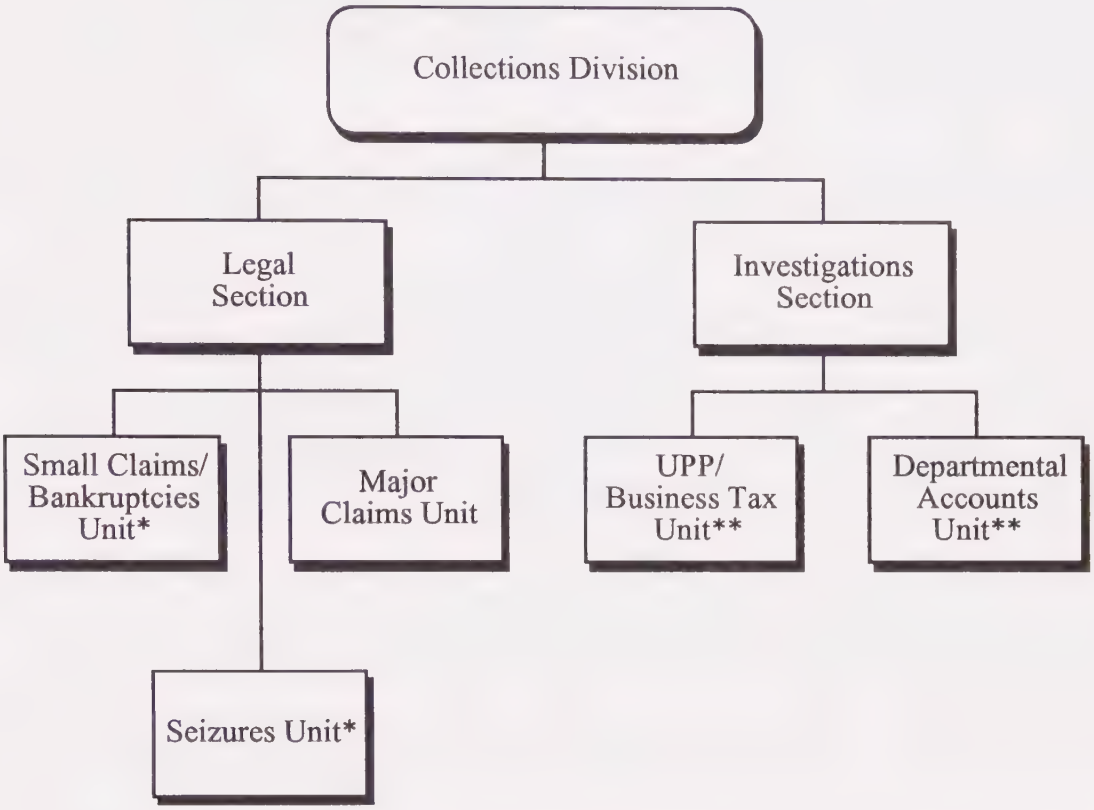
PROPOSED REORGANIZATION OF DELINQUENT REVENUE COLLECTION ACTIVITIES

Our proposed organization for delinquent revenue collections is summarized in the following paragraphs.

The Investigations Division, the Bureau of Delinquent Revenue, and the Legal Division should be consolidated under a single manager. Within this Division, the Tax Collector should establish an Investigations Section and a Legal Section. Employees in the Investigations Section should be divided into specializations — business and UPP tax, and medical bills — according to the resource requirements established by the prioritization system described below. However, employees should be cross-trained to enable a single investigator to collect from entities owing more than one type of delinquent revenue. The Legal Section should include a Seizure Unit and a Small Claims/Bankruptcy Unit that are not staffed by lawyers (lawyers may not file small claims) and another Unit including attorneys pursuing larger claims. Collection letters and account modifications would be conducted outside of the Collections Division, by the Accounts Services Division. The following organization chart indicates the proposed new organization structure.

Chart 10

Recommended Collections Division



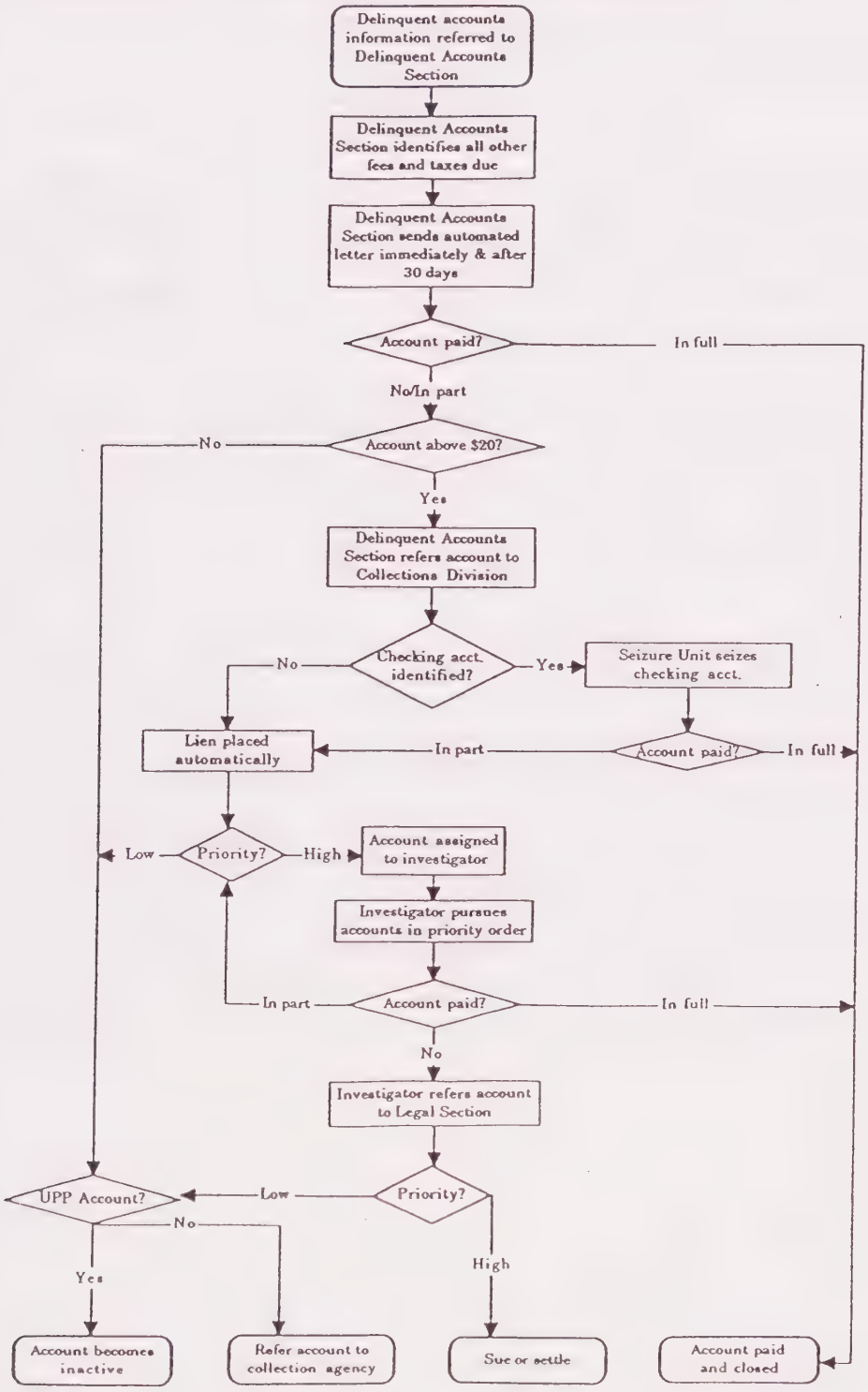
* Small claims/Bankruptcies personnel should be cross-trained with Seizures personnel for maximum flexibility.

** UPP/Business Tax personnel should be cross-trained with the Departmental Accounts personnel for maximum flexibility.

The flow chart below depicts the ideal process by which the Tax Collector would collect delinquent revenue.

Chart 11

Proposed Flow of Collection Activities



The Tax Collector should proceed through the flow of activities indicated in the above flow chart in accordance with the appropriate responses to the decision points (depicted by the diamond-shaped boxes). It is important to note that we are recommending that the Tax Collector implement an identified flow of delinquent revenue related activities. Currently, there is no flow of activity, instead, individuals and divisions behave independently, without recognizing their roles as part of a larger system. The flow chart above includes the following important elements.

- Every delinquent account holder should receive a minimum of three consolidated notices, including the entire amount owed, before any additional action is taken;

- The Tax Collector should implement a prioritization system and rank each delinquent account after any payment is received. Low priority accounts should be referred to a collection agency or, for UPP, be made inactive. Higher priority accounts should be pursued in order of importance. The Legal Section should implement a prioritization system as well. CUBS, which has been newly acquired by the Tax Collector, can be used to automate such a prioritization system; and

- Non-labor intensive, effective delinquent revenue techniques should be implemented prior to labor -intensive techniques. Specifically, the Tax Collector should seize checking accounts before any in-person visits are made.

A detailed explanation of each of the activities included in the flow chart are contained in Appendix B.

IMPLEMENTATION

The suggested reorganization of collection activities, above, represents a substantial departure from present activities. As such, certain barriers to implementation will need to be overcome, and full implementation may be realized over a period of years. The following paragraphs describe some anticipated barriers to implementation, suggest ways in which these barriers can be overcome, and make recommendations for implementation priorities.

To summarize some of the differences between current practices and our recommended new collections methods:

- We recommend preparing consolidated delinquent accounts statements, so that, whenever the Tax Collector makes a collection attempt, he attempts to collect for the entire amount outstanding for all revenue types. Currently, delinquent revenues are pursued separately. An Investigator visiting a business to collect delinquent UPP taxes does not, necessarily, request delinquent business taxes at the same time.

- We recommend mailing two letters listing the total amount of delinquent revenue owed, thereby allowing the delinquent accountholder an additional opportunity to pay initially through the mail. Currently, letters are not mailed to delinquent accountholders automatically (although some BDR staff persons do mail letters at their discretion).

- We recommend seizing checking accounts to collect all types of delinquent revenue. Currently, only BDR seizes checking accounts to collect delinquent hospital bills. The Investigations Division makes in-person visits to collect delinquent UPP taxes, and does not make delinquent business tax collection a priority.

- We recommend that the Tax Collector establish a delinquent accounts prioritization system in cases where mailed notices and checking account seizure are insufficient to recover the full cost of the debt. Currently, the Investigations Division has established a type of tax — UPP — as a priority, rather than prioritizing accounts individually based on the likelihood of maximizing revenue and the goal of promoting voluntary compliance from all types of taxpayers. We also recommend that the Legal Section apply a similar prioritization system, when such a prioritization system is not in place in the Legal Section.

- We recommend that all functions in the legal sphere — i.e., seizures, small claims, bankruptcy, and major claims — be consolidated under a Legal Section with attorney oversight. Currently, small claims and bankruptcy proceedings are limited to departmental accounts (mostly hospital bills) in BDR and have no legal oversight.

Because our recommendations differ substantially from current practices, and because implementation of these recommendations will happen over time, we are unable to make specific recommendations regarding resource allocation at this time. However, we do have some general recommendations in this regard.

The Delinquent Accounts Section of the Accounting Division (See Section I.1 of this report) will be performing an entirely new function, although this function is closely related to the Clearance Unit of the Investigations Division. As noted above, the Clearance Unit, which includes six FTEs, compiles consolidated accounts information for all businesses attempting to register, and withholds registration certificates for businesses with any outstanding revenue. However, the Clearance Unit does not calculate interest and penalties. Neither does the Unit compile consolidated account information for delinquent accountholders.

The Tax Collector should transfer the Clearance Unit personnel from the Investigations Division to the Accounting Division's Delinquent Accounts Division. In addition, the Investigations Division and BDR each have an Accounts Clerk; these two FTEs should be transferred to the Delinquent Accounts Section. However, because calculating penalties and interest, entering the consolidated accounts information into a new database, and implementing mailings are entirely new functions, it is possible that these resources will be insufficient to carry out all of the

responsibilities of this Delinquent Accounts Section of the Accounting Division. In addition, the Tax Collector has expressed concern that implementing delinquent accounts mailings will result in large numbers of telephone calls from delinquent accountholders.

If the two Accounts Clerks and the six Clearance Unit personnel are insufficient to produce consolidated statements, implement mailings, and respond to telephone calls, the Tax Collector should transfer additional collections and Investigations staff to this unit, at least on a temporary basis, until this function is fully staffed: as noted above, mailing statements to all delinquent accountholders as quickly as possible will result in the most revenue per Investigator, because: (1) this activity is not labor intensive; and (2) the more recent a delinquency, the more likely it is that the delinquency will be collected.

Similarly, the Seizure function of the proposed Collection Division is entirely new, and should be fully staffed before the Tax Collector allocates any resources to Investigators with individually assigned accounts. Again, this function is less labor intensive, and collects from delinquent accountholders quickly, before an account becomes stale. Resources should be assigned to individual telephone and in-person pursuit only after mailing consolidated statements and seizing checking accounts are fully staffed.

If, after this proposed reorganization has been in place for a year or more, the Tax Collector determines that he requires additional personnel to implement all of the functions on the above flow chart, the Tax Collector should present a substantiated request to the Board of Supervisors. This request should quantify the time spent by collections personnel on consolidating accounts, mailing letters, responding to telephone calls, and placing seizures, and should also detail the number and amounts of accounts still outstanding, after these activities are completed, and the Tax Collector's anticipated revenue from adding staff to implement individual telephone and, in rare cases, in-person pursuit.

Based on an average annual collections for all three units of approximately $15 million, and a conservative one percent increase in delinquent collections as a result of these recommendations, the Tax Collector will realize additional annual revenue of $150,000. Based on a less conservative ten percent increase in delinquent collections, the Tax Collector will realize additional annual revenue of $1.5 million.

SUMMARY

We found various problems with the Tax Collector's methods of collecting delinquent revenue. Currently, three separate divisions of the Tax Collector's Office are responsible for delinquent revenue collection. If an accountholder owes more than one type of delinquent revenue, collections personnel pursue these various outstanding debts separately. Tax Collector personnel use labor intensive collections methods: letters are not mailed to delinquent accountholders automatically (although some BDR staff persons do mail letters at their discretion); only BDR seizes checking accounts and the Investigations Division makes in-person visits to collect delinquent UPP taxes. The Tax Collector has not established a prioritization

system to ensure that accounts that would likely result in the highest return are pursued first. Functions in the legal sphere — i.e., seizures, small claims, bankruptcy, and major claims — are performed in separate locations, without legal oversight except in the case of major claims.

RECOMMENDATIONS

The Tax Collector should:

1. Consolidate the Investigations Division, the Bureau of Delinquent Revenue, and the Legal Division under a single manager, organized in conformance with the recommendations contained in this report;

2. Mail two notices to delinquent accountholders reflecting the total outstanding amounts owed and informing them that failure to pay in full will result in future action by the Tax Collector;

3. Seize the financial assets, particularly checking accounts, of delinquent accountholders (this recommendation may only be implemented for business taxes if the Board of Supervisors approves an ordinance allowing the Tax Collector to do so - see below);

4. Place liens on the person and/or property of delinquent accountholders automatically;

5. Establish a prioritization system for the collection of delinquent revenue, ranking them by collectability, amount, and time limitations;

6. Fully staff initial collections functions before allocating any resources to later functions, in the following order: delinquent notices, then seizures, then liens, then accounts assigned to individual Investigators; and

7. Issue citations demanding full payment of delinquent accounts or attendance at a Tax Collector's Administrative hearing, including a fine that fully recovers the Tax Collector's costs for issuing the citation.

The Board of Supervisors should:

8. Approve an ordinance allowing the Tax Collector to seize the checking accounts for businesses with delinquent Business taxes; and

9. Approve an ordinance enabling a limited number of Tax Collector Investigators to obtain Peace Officer status as an additional enforcement tool.

COSTS/BENEFITS

Costs would be based on the Tax Collector's substantiated need for increased personnel. Implementation of the recommendations contained in this report would result in estimated increased revenue of $150,000 to $1.5 million annually.

Office Of The Treasurer/Tax Collector

City and County of San Francisco
Mailing Address: P.O. Box 7426 ❖ San Francisco, CA 94120-7426
Street Address: 875 Stevenson Street, 2nd Floor ❖ San Francisco, CA 94103

MARY I. CALLANAN, Treasurer
Phone: (415) 554-4478

RICHARD A. SULLIVAN, Tax Collector
Phone: (415) 554-4470

April 20, 1995

Through: Mary I. Callanan, Treasurer

Mr. Harvey Rose, Budget Analyst
San Francisco Board of Supervisors
1390 Market Street, Suite 1025
San Francisco, CA 94102

Dear Harvey:

Enclosed is the Tax Collector's response to the Management Audit your analyst conducted. We feel, however, that it would have been helpful to have more time to respond to an audit that took several months to complete. As you know, we do not totally agree with certain sections of your report. However, I find many of the observations and recommendations useful and some of them will be utilized in my ongoing restructuring effort.

Please thank the audit team, particularly Debra Newman, for conducting themselves in such a professional manner.

Sincerely,

Richard A. Sullivan
Tax Collector

Enc.

Tax Collector's Response To Budget Analyst's Audit

Introduction

First of all, I thank the audit and consulting team for their professionalism and willingness to listen to our concerns. The members of the team, led by Debra Newman, are Karen Sikkenga, Eve Sternberg, Debra Ward, Susan Maher, and Lauren Nadler. We appreciate the methodical and reasonable approach with which they addressed this demanding task.

In analyzing the report, I am pleased to find that the Budget Analyst recognizes and supports our efforts at restructuring and at Total Quality Management (TQM). I had already begun these efforts, even before my tenure as Tax Collector started on July 1, 1994. The support of the proposals to centralize Taxpayer Assistance, (TQM report "Bravo"), and to centralize accounting and statement processing, (TQM report "Charlie"), is very welcome.

Many other areas of the audit report and recommendations reflect other efforts and accomplishments since my tenure as Tax Collector began. Two examples are (1) the purchase of scanners to improve Business Tax Statement processing, and (2) passage of legislation to eliminate the small business exemption for non-filers in order to make the determination process more realistic.

The audit report is the result of a review of the operation of the Tax Collector's Office conducted over several months by a team of auditors. It is a comprehensive and detailed study, worthy of a detailed review and response. Lacking the time needed for an effective, in-depth study of all of the issues raised, our responses are necessarily somewhat general in some areas, and more specific in others.

The Budget Analyst has identified areas of great concern to us which we have already begun to address. We do not totally agree with some of the projections that he has made regarding lost revenues as a result of unregistered businesses, and we explore our reasons for questioning these projections in the following section by section comments. But, to put the issue in perspective, the amounts put forth by the Budget Analyst in his introduction represents a range of, at a minimum, 0.7 % and at a maximum, 1.6% of our total annual revenues.[1]

COMPLIANCE ENFORCEMENT

Prior to 1978 (before Proposition 13 and the Small Business Exemption), the Tax Collector's Office had four investigators responsible for registration enforcement. These employees conducted field visits and yellow page surveys. The Board of Supervisors created the Small Business Enterprise Exemption. Staffing was cut. The compliance

(enforcement) unit was reduced to one investigator and the others subsequently dispersed to other programs. The obvious decision was to maximize revenues by establishing such priorities as pursuit of delinquent Unsecured Personal Property Taxes that could be addressed by a shrinking staff. Auditors were designated to look for obvious scofflaws.

Exhibit #1 shows staffing of the Investigations section from FY 90-91 to the present. That these priorities have been successful is shown in Exhibit #2 which reveals a steady increase in Delinquent Collections by the Investigations Unit for the last five years. We are pleased to see the Budget Analyst recommend establishment of a separate business registration unit. This is exactly what we have felt all along would be the most effective way to enforce registration.

LEGISLATIVE ISSUES

Changes in tax legislation have had significant and far reaching effects on the Tax Collector's operation, as acknowledged by the analyst in the report. The Tax Collector has been charged with the implementation and execution of 21 new local ordinances during the three year period between February, 1992 and February, 1995, without any significant increase in staffing. In fact, 17 of these local ordinances were approved during the 15-month period from May, 1993 through July, 1994.

Implementation of these changes delayed development of the Business Tax (BTS) System for over a year. BTS was expected to address, in this year, the following areas that are a major concern of the Analyst: Automated audit selection; a more comprehensive non-filer determination process; development of training modules; and more effective utilization of employees, to name but a few. Before the audit/consultant contract began, we had already identified these as areas that needed our attention. We had visualized and began developing the BTS system over ten years ago, but funding was withheld over and over again.

STAFFING ISSUES

In order to put the Budget Analyst's report in proper prospective, one must have some general understanding of the difficulties of managing in the public sector, particularly during the last six years. Enormous effort must now be expended to overcome seemingly endless hurdles in order to get things done. For example, in several locations throughout the report, mention is made that all vacant positions must be filled as soon as possible. There also is a suggestion that a new classification should be established for individuals to staff the Taxpayer Assistance Unit.

The hiring process is a major stumbling block. Despite repeated requests, reminders and cajoling, requests to hire are mired in the City's hiring process for months on end. This is particularly stressful in light of the fact that most of the vacancies are potentially revenue-producing or will release people from performing administrative work to revenue producing activity. Furthermore, we must conform to Civil Service rules, hiring standards and procedures that are often convoluted and time-consuming. It would have been helpful to stress in the summaries that various constraints, such as the City's hiring process, with which we must comply, often offer significant obstacles and that this should be examined on a City-wide basis.

Another problem is the process for the development of a new classification, as suggested for the Taxpayer Assistance unit. This may well be the best approach, but it should be recognized that this can take years and the process is daunting.

Roughly the process is as follows: Human Resources must study the duties of the new classification, develop a job description and an appropriate examination. The positions must be approved in the budget. The department must prepare requests to hire. The appropriate offices must approve the hire, i.e., the Mayor's Office, the Controller and the Human Resources Department. The vacancies must be advertised widely. Applications must be screened and candidates notified. The exam must be given and a list established. Results must be certified, the list posted, candidates notified of the results and given opportunity for protest. Successful candidates are interviewed. Selection is made from the list and individual(s) hired. Appointments to the positions are made and processed, and employee(s) given orientation to the department. This takes a long time.

FISCAL CONSTRAINTS

San Francisco is in its sixth (6) year of declining resources and severe budget constraints. It is estimated that next fiscal year, the budget deficit will be over $100 million dollars. The Tax Collector's Office has been adversely affected as have most operating departments. See Exhibits 3 and 4 for the Treasurer/Tax Collector's ten year budget and revenue comparison.

These constraints have unquestionably affected our ability to accomplish some substantial and much needed changes, such as development of a department-wide consolidated taxpayer database and increased tax audit activities. When resources are reduced, discovery and enforcement programs (surveys and audits) are necessarily restricted, as auditors and investigators are reassigned to general office duties.

As you can see from the attached Exhibits, the rise and fall of our Budget and employee count has been like being on a roller-coaster. Personnel turnover and City wide bumping, when lay-offs occur, have been particularly damaging to many discretionary activities (Business Tax Surveys and Audits) as staff time is diverted to more immediate issues. (See Exhibit 5). Our budget narratives in the past have pointed out a direct correlation between levels of enforcement activities and taxes collected. The Budget Analyst's audit, in my opinion, validates this point.

SUMMARY

In summary, as I stated earlier, I question the amount of uncollected revenues projected by the Budget Analyst. Our reasons for challenging those projections appear in the following section by section comments.

Finally, I want to emphasize that we had already identified and begun to address many of the issues that appear in the body of the audit report prior to the Budget Analyst's review. We will note these various issues as we comment on each operational section in the body of our response to the document.

SECTION I.1: Accounting and Statements

We agree that, as proposed by Task Force Charlie, centralization of the check control and accounting function is desirable. However, it must be done in a fashion that will achieve **maximum efficiency and savings** to the city while maintaining the **same level of service** to the taxpayer.

SECTION I. 2: Automation

We agree with many of the comments in this section, except the assertion that the new Business Tax System (BTS) is "going to waste".[2] In order to appreciate the effectiveness of this system, you would need to know the restrictions of the former system. In the past, the Treasurer/Tax Collector Department was unable to respond promptly or efficiently to requests for analysis. It was not possible to capture sufficient data to discover a taxpayer's total liability. As a consequence, more business "escapes" took place than under this new system.

This new system captures all Business Tax data using the SSN or the FEIN. This was not possible before. Now all information relevant to the taxpayer is in one place because we have **linked** all types of business taxes, (e.g. Business Payroll, Parking, Hotel Tax) into one account.[3] This makes it possible to identify more efficiently and completely the full Business Tax liability of an individual taxpayer. The result has been increased revenues for the city, especially in the area of Accounts Receivable.

The report comments on access restrictions to this system and suggests that training is too brief and narrow in scope. Initially, training and access were limited because of the complexity of the system itself and because of immense staffing problems due to turnover, early retirement, and budgetary constraints. Users of the BTS were specifically trained in their areas of responsibility. Additional training was presented on a continuous basis as enhancements were implemented and as staff replacements came aboard.

One must allow for the fact that the system employs 110-115 individual "screens". To train every employee in the use of every screen would be not be cost-effective. An individual will use some screens every day and some screens never at all. This all depends upon the person's responsibilities. When the employee needs access to fulfill new or changed responsibilities, training and access are given. Given the complexity of the system, we would agree that additional training and periodic refresher training would be beneficial to staff and this was already planned. The first session in a new series of training was conducted in February, 1995.

Several formal groups, including the BTS Steering Committee, BTS Sub-Committee, and a number of topic-specific task forces, met throughout the multi-year development and implementation cycle to discuss issues, formulate policy and procedures, and make participatory decisions. Training was based on function, and the decision to restrict functions at different levels was made based on the strong recommendations of the Controller's Internal Audits staff due to the confidential nature of the information in the files.[4]

It is not true that end-users of custom software have no effective input into the design, installation, or modification of such software.[5] In fact the end users are the primary decision-makers, working closely with Controller's I.S.D. on these issues. As stated above, Business Tax staff was integrally involved in all aspects of the BTS development and implementation. In addition to the formal groups described above in which decisions were made, a Senior Auditor was assigned for almost two entire years as a member of the BTS team, and was relieved of audit assignments in order to work with the programmer/analysts on design and implementation of the system.

In addition to Business Tax, staff from all other sections of the department were required to participate actively in the design process over several years, and regularly took part in **Structured Walkthroughs** - formal presentations of work done by the development team, with formal signoff by all participants. All documentation on staff participation, and all signoff sheets from the walkthroughs, are available from both the Tax Collector and the BTS Team in Controller's I.S.D.

Through our weekly BTS subcommittee meetings, training needs and end user concerns are discussed. Priorities are established and acted upon in order as restricted resources permit. This group is the most knowledgeable concerning the way the system was designed and launched. They are, therefore, in our opinion, best able to make these kinds of decisions. The BTS subcommittee's meetings are open to all interested end-users. The minutes and agendas are distributed to no fewer than 20 staff members for input and feedback.

Linked databases would be an enormous productivity tool for all sections. This has been a goal of the Tax Collector's staff for several years, and we have tried in many ways to implement this goal. We participated actively in the **PROMIS** Steering Committee - a city-wide property system development project of I.S.D. that was sponsored by the Assessor's office and endorsed by multiple departments which were going to use it as a focal point to link databases throughout the City. Unfortunately, PROMIS was canceled by the previous Assessor when he came to office.

In addition to PROMIS, linking the BTS with our UPP and License files was part of the original BTS design, in a module called *External Interfaces*. We have not yet been able to implement this module due to:

1. Funding difficulties - we are in our sixth deficit year and were forced to defer this functionality in order to address more pressing priorities.

2. Constraints imposed by I.S.D. as our service provider, which uses older flat-file technology that is not conducive to the database connectivity we need, and which claims that migrating these files to database technology would be prohibitively expensive.

3. The likelihood that the Assessor will choose a new property system database within the next 24 months, which would make it inadvisable to spend money modifying unsecured personal property tax files that would be replaced by their new system.

The addition of six new positions was approved in the FY 94-95 budget for administrative and clerical staff in the Business Tax section. This will now give us the opportunity to revisit and correct any existing inefficiencies. Please note that many of the points made in this audit report were already being addressed by the Treasurer/Tax Collector Department.

We realized that adequate support staff to monitor automation was a key to effective utilization of its potential. Prior to this fiscal year, we had only one MIS position, an 1818 Management Information Systems Specialist II. A second position, an 1819 Management Information Systems Specialist III, is in the process of being hired. This was done by reclassifying an 1844 Sr. Management Assistant at the time of the incumbent's retirement in December, 1994. A third position, another 1818 Management Information Systems Specialist II, was approved in the FY 94-95 budget, but is still in the classification process and, therefore, unfilled at this writing.

SECTION I.3: Taxpayer Assistance

We agree, in large part, with many of the recommendations regarding Taxpayer Assistance that appear in this audit report. These issues were certainly known to us and were thoroughly explored by the management group and by Task Force Bravo which was established by the Tax Collector to explore Taxpayer Assistance issues. We also greatly appreciate the section concerning the Tax Collector's efforts and accomplishments and the mention in the opening summary of the *Taxpayer Assistance* section, in which the recommendations of Task Force Bravo are endorsed.

The management group recognized at the outset that a centralized Taxpayer Assistance unit is a necessity, if maximum efficiency is to be achieved and has continued to move toward establishment of such a unit. It should be noted, however, that the centralized Taxpayer Assistance unit will not totally relieve other employees of the need to assist taxpayers. Other employees will be utilized as specialists who backup the generalists when the problem is more complex. The eighty /twenty rule will probably apply here. Eighty percent of the inquiries can probably be handled by this small unit, but the remaining twenty percent will require the expertise and assistance of the remaining staff in the different sections.

Several references are made throughout the document that rotational staffing to the Business Tax assistance desk is ineffective and bad for morale and it is urged that this be addressed. This staffing problem has now been addressed with a permanent staff and supervisor in the Business Tax section. The suggestion of cross-training is a concept extensively discussed in management group and further developed and recommended in Task Force Bravo. Such training has already begun with Taxpayer Assistance representatives from several sections and is slated to be presented to every single member of the department.

In the report, it is noted that no final decision has been made regarding a separate, consolidated taxpayer assistance unit. Actually, this decision has been made, and implementation begun, but decisions regarding the necessary physical setup had to be deferred because of the Department's move from City Hall. It was necessary to agree to a new floorplan at the new location before any details of a new physical arrangement could be developed. 6

SECTION II.1: Licensing

The Tax Collector agrees that the recommendation of combining billing activities for license fees is a desirable goal. However, before considering any major changes, priorities must first be established. We must take into account the direct impact of these recommendations on the ability of the Treasurer/Tax Collector Department to function and the effect that they will have upon taxpayer service and upon interacting departments.

An implementation target of FY 96-97 has been suggested,[7] but this may be extremely difficult in the light of all of the underlying tasks which must be accomplished in order to make these sweeping changes possible. To hope that this would be completed within one year may be optimistic. Before implementation, many issues must be addressed:

1. A large number of ordinances and codes must be changed through the legislative process in order to enable such consolidation. Legislative change is, at best, a complicated and time-consuming process. It is sure to require considerable staff time on the part of the Tax Collector's office and from staff of assorted legislators, and heads of other departments affected by various aspects of this venture.

2. Some businesses require multiple permits and licenses which are issued on different timetables. An example is establishment of a dance hall. Separate aspects of such an operation are regulated under the authority of the Fire, Heath and Police Departments. Without these legislative modifications, most proposed changes cannot occur at all.[8]

3. A second major problem is synchronizing the existing payment schedules. For example, Food Preparation and Service businesses are mailed statements in March of each year. This will not easily mesh with program cycles or with billing procedures and deadlines already established for Business Tax and Property Tax Sections. In order to bring all of these into synch, it may be necessary to make drastic adjustments to certain billing cycles. The first year we may need to skip certain billing deadlines, causing lost revenue, or accelerate the billing cycle by sending the next year's bill a few months after the last one. This is sure to irritate affected citizens.[9]

4. User departments' response. Most departments schedule billings and collections throughout the year for manageability and workflow control. Sending the billings out simultaneously will cause an unwieldy volume of response that will result in processing delays which may have legal ramifications for the department. For example, it is necessary to meet the Controller's timeframe for special assessments.[10]

5. The sheer mechanics of designing and testing the operative computer program will very likely result in an unacceptable time lag and in significant modification and maintenance costs. This again makes the one year implementation timetable far from feasible.[11]

6. Property owners may well respond negatively. Additional fees attached to the property tax bill could create a financial burden which will result in lower compliance levels and reduced revenues.[12]

7. We feel that the current level of staffing is unlikely to be affected. The work of processing over 150 different fees and licenses will still exist. It is reasonable to assume, however, that present employees may be reassigned to more pressing duties in other sections as part of the Department's restructuring effort. Employees may be reassigned to other areas of collections and to the Taxpayer Assistance Unit which is in the implementation stage.[13]

8. DPW and the Rent Board collections reach at least 90% of its maximum collection by the first quarter of each billing period. Combining these two collections the first year of implementation with the Property Tax statement would create a cashflow, <u>not additional revenue</u>. Of the remaining amount, approximately eight percent is collected the following year as delinquent accounts.[14]

The Treasurer/Tax Collector Department has already established the goals of creating a dedicated taxpayer assistance unit, developing a much needed centralized billing and accounting section, and of providing training for staff in the proper use of the existing computer systems. These three goals, with which the Budget Analyst concurs, will substantially improve the operations of the Tax Collector's Office. Once these changes are in place, service to taxpayers should improve and collections are expected to be maximized.

Because the consolidation of licensing is unlikely to be accomplished in one year, it is our firm belief that it is imperative to address the three goals listed above. It is administratively sound to focus first on those operational aspects which will achieve the greatest impact in the shortest amount of time. Since, as the Budget Analyst has observed, there are no major shortcomings in the administering of licensing activities, consolidation of this function should be considered as a long range goal. Adding major changes to existing operations without completing and evaluating the success of our restructuring program is not the immediate answer.

SECTION II.2: Dog Licenses

We are in general agreement with the concept of turning over the processing of dog licenses to the Department of Animal Care and Control and propose no modifications.

We feel, however that the proposed budget reduction is far too high and will adversely impact other aspects of the present License program, regardless of the final disposition of this unit. The work of processing over 150 different types of fees and licenses will go on. The portion devoted to serving the dog license alone is minuscule by comparison.

It should be noted that the Tax Collector has nothing to do with either the staffing or the budget of the Department of Animal Care and Control.

We do feel that the estimate of a dog population of 177,000 is questionable.[15]

SECTION III. 1: Business Tax Auditing

Many of the findings reported in this section of the Budget Analyst's audit report are known to the Business Tax staff and we have already taken steps to effect change. For instance, the report notes that "the division has begun to implement this redirection of auditors to focus them on audit activities, and the decline began to reverse itself in FY 93-94."

We also note that the report acknowledges the beneficial effect of our Taxpayer Assistance Unit's reorganization which was initiated in February, 1995. The automated audit selection system developed with the assistance of Controller's ISD staff is now ready for implementation.

We are confident that through the reorganization of the division units, redirection of audit focus, automated audit selection, and utilization of a more efficient telephone system, we can improve audit billings as suggested in the Budget Analyst's report.

SECTION III.2: Review of City Park Audit

The Budget Analyst suggests that the Business Tax Audit staff used methodology in the City Park audit that is not supported by work papers and that resulted in an audited deficiency billing that was $35,574 less than if the existing methodology, developed by the City's Department of Public Works (DPW) had been used.

The Tax Collector strongly disagrees with these assertions. The review of parking operations at Candlestick Park was complex, time-consuming, and forensic. To fully appreciate the complexity of the review, one must recognize that:

- DPW placed a great deal of reliance upon the results of a traffic flow study which they performed approximately ten years ago.[16]

- None of the peripheral lots surrounding the stadium lot had paved or marked stalls.[17]

- The peripheral lots were operated by different lessors. One of them allowed employee parking during ball games.[17]

- The number of cars parked in the peripheral lots depends on game attendance, weather and parking lot conditions, public transportation schedules, available on-street parking spaces, the day of the week, the sport being played, the team's current win-loss record, and the opposing team.[18]

In attempting to apply a formula developed ten years ago, and with so many variables involved, it was not possible to ascertain the exact number of cars parked for each ball game. Recognizing these difficulties, we nevertheless used the DPW methodology, with a minor correction. The correction was made to rectify DPW's inadvertent (and unexplained) matching of cars parked on the October 13, 1994 game with the lower attendance of 58,050 on September 29, 1985 rather than the actual attendance of 60,582 for that day.[19]

Partly to validate the corrected formula and partly as a follow-up of our audit, we conducted a series of surveys of the Candlestick peripheral lots in late 1994, when the football season resumed. The results of these surveys, (see chart on page 17), strongly indicate that the corrected formula used by the Tax Collector is more fair and reasonable than that used by DPW. The third survey was incomplete.[19]

The Budget Analyst implies that the Business Tax audit staff neglected to assemble the complete working papers necessary to establish an audit trail, to permit thorough supervision by senior staff auditors, or to permit review by any experienced auditor.

For reasons that are not entirely clear, the Budget Analyst's staff reviewing the City Park audit did not review the complete workpapers.[20] The workpapers pertaining to the Tax Collector's adjustment of the DPW formula and the 1993 payroll tax audit of City Park were not among the workpapers reviewed by the Budget Analyst's staff.

We are convinced that all workpapers prepared by the Tax Collector audit staff have been properly assembled and cross-referenced and that any person reviewing the complete set of workpapers should have no difficulty understanding our methodology.[21]

In the report, the Budget Analyst erroneously stated that 3,288 employee vehicles (of Tuntex) were subtracted from a Sunday game. The credit adjustment of 3,288 cars was not for employee vehicles parked on Sunday, but for cars parked during the period the lot was managed by a different operator (Metropolitan Parking) for Tuntex, the lot owner. This was explained as a footnote to Exhibit VII of our audit report.[22]

General Comment: The Business Tax section launched a comprehensive audit of San Francisco Parking, Inc. (City Park) in February, 1994, amidst a host of innuendoes of wrong-doing and allegations that perhaps as much as $10 million in parking tax revenues might have gone uncollected.

To insure that the audit was conducted with the highest degree of professionalism and integrity, the audit was conducted in full compliance with the U.S. General Accounting Office's (GAO) Auditing Standards. The types of audits applicable by these standards were financial and performance audits.

We were certainly conscious of the publicity and controversy surrounding the account and were aware that our efforts would come under the closest scrutiny. While planning the audit, we made every effort to insure that assigned audit staff were free of any personal or professional involvement that might tend to hinder an objective and independent audit. We wanted to avoid any hint or appearance of impropriety. To further that end, we assigned a principal auditor who had no prior involvement with the account and who also met the necessary qualifications to perform such a complex audit.

This comprehensive audit started in February, 1994, with a principal auditor as Auditor-in-Charge and two staff auditors. The project took three months of staff time to complete. Their examination consisted not only of the parking tax, but also of business and payroll tax liabilities for all of the taxpayer's parking operations in the city and at Candlestick Park for a period of three years. The financial and payroll audit included a review of the taxpayer's federal and state corporate returns, DE-3 returns filed with the state Employment Development Department, trial balances, and other pertinent documents.

We believe that the results of our audit of City Park's operations at the downtown San Francisco locations and at Candlestick Park were reasonable and fair, and based on sufficient, competent, and relevant evidence.

Tax Collector Survey and Follow-up -- City Park Audit

Date: Oct. 2, 1994 (vs. Philadelphia)	Act. per Survey	DPW Method	T/C Formula
1. Turnstile Attendance	64,771	64,771	64,771
2. Est. % of persons-trips by private cars	N/A	81.80%	80.00%
3. Total arriving by private cars (#1 x #2)	N/A	52,983	51,817
4. Est. persons per car ratio	N/A	2.67	2.73
5a. Actual car count of aerial photo	19,320		
5b. Est. # of cars parked in per. lots (#3/#4)	N/A	19,844	18,981
6. **Difference** (#5a - #5b)	0	524	339

Date: Oct. 23, 1994 (vs. Tampa Bay)	Act. per Survey	DPW Method	T/C Formula
1. Turnstile Attendance	62,741	62,741	62,741
2. Est. % of persons-trips by private cars	N/A	81.80%	80.00%
3. Total arriving by private cars (#1 x #2)	N/A	51,322	50,193
4. Est. persons per car ratio	N/A	2.67	2.73
5a. Survey of cars parked incomplete			
5b. Est. # of cars parked in per. lots (#3/#4)	N/A	19,222	18,386
6. **Difference** (#5a - #5b)	0	Not Available	Not Available

Date: Nov. 13, 1994 (vs. Dallas)	Act. per Survey	DPW Method	T/C Formula
1. Turnstile Attendance	69,014	69,014	69,014
2. Est. % of persons-trips by private cars	N/A	81.80%	80.00%
3. Total arriving by private cars (#1 x #2)	N/A	56,453	55,211
4. Est. persons per car ratio	N/A	2.67	2.73
5a. Actual car count of aerial photo	19,484		
5b. Est. # of cars parked in per. lots (#3/#4)	N/A	21,144*	20,224
6. **Difference** (#5a - #5b)	0	1,660	740

* Exceeds maximum capacity of 20,945 cars for combined peripheral lots.

SECTION III. 3: Business Registration

In the course of their study of the Tax Collector's Office, the audit team visited five commercial buildings. The data collected indicated that of the 359 businesses surveyed, a total of 206 businesses (57%) were registered by the Tax Collector and that 153 (43%) were not registered. By combining this survey with other estimating methods, many of which are understated or overstated in various ways, the budget analyst concluded that the number of unregistered firms doing business in San Francisco might be anywhere from 9,000 to 53,000. Based upon this broad range, the Budget Analyst estimated that the City and County of San Francisco may be losing up to $6.8 million annually in business registration fees.

We feel that the sampling method employed was neither statistically random nor sufficiently large to be representative, as the Budget Analyst acknowledges in his report.[23] As a consequence, the projection of 53,000 unregistered businesses is perhaps somewhat overstated.[24] The following facts, obtained from other comparable sources, shed some doubt on this projection.[25]

Source	# of Businesses in Database
Tax Collector BTS System	64,951
EDD Employer Files	27,500[26]
Assessor Business Files	54,470 (Excl. 5,208 apt. ownerships.)

We conducted our own random survey of three downtown buildings (One Embarcadero Center, Two Embarcadero Center, and 525 Market Street), which may be slightly more representative than the Budget Analyst's sample.[27 & 28]

Based on the tenant's list supplied by the buildings' property managers, the Pacific Bell Street Address Telephone Directory, Building Directory listings, and the Tax Collector's BTS records, we identified a total of 179 businesses at these three locations. Of the 179 businesses, 160 were registered with the Tax Collector and 10 were not. Nine other businesses were insurance companies and financial institutions and were not required to be registered. Based on these results, we found a 93.75% rate of registration compliance at the three aforementioned locations.[29]

Since both the Tax Collector's and the Budget Analyst's survey results were based on somewhat tenuous samples, the results are a bit speculative and should only be used as a guide.

Admittedly, there are unregistered businesses in a number of downtown buildings. However, this unknown number is more likely to be at the low end of the Budget Analyst's estimate. In order to focus on discovering unregistered businesses, the Tax Collector hired three collection officers at the beginning of the year and has assigned them to the Investigations section.

The Budget Analyst has suggested that the Tax Collector establish a designated Business Identification unit in the Business Tax section with responsibility for identifying and registering businesses in the city.

The Investigations section already has the responsibility for identifying and registering unregistered businesses and for conducting periodic surveys in search of unregistered businesses. Investigators have done surveys within the financial district as well as the outer areas of the city. Attention was temporarily diverted from this effort by the creation of the Clearance Unit. This unit was created for the purpose of insuring that all businesses pay all outstanding taxes before being issued a certificate of registration. This unit also participated in the registration of unregistered businesses, but was somewhat diverted from this effort by the start-up of the BTS system.

Another disruptive element was the creation and initiation of the TBAI and TBAX systems. These were developed to provide ready access to various UPP accounts and to provide a snapshot view of current and all prior delinquent personal property tax years. A major objective was to collect all prior delinquent tax and simultaneously reduce assessments on the UPP roll. Another objective was to reduce personal property delinquency to 2%. Currently, there are approximately 40,000 delinquent outstanding accounts on the roll.

The Tax Collector has already determined that a cost-effective program designed to detect unregistered businesses would require participation in an exchange of information agreement with other taxing entities. However, the Tax Collector also welcomes the recommendation of a designated unit to register previously unregistered businesses. The Tax Collector's Business Tax section has been working with the State Employment Department and the Franchise Tax Board since 1993 to enter into an exchange program without a very formal procedure being established.

Although no positive response has yet been received from the state, the California Municipal Business Tax Association has advised the Tax Collector's Office that they are close to an agreement with the Franchise Tax Board to enable the Board to reciprocate by sharing tax files with cities under the SB 90 program.

We believe that the majority of unregistered businesses would only owe either the $25 or $150 registration fee as the downtown building surveys suggest. Aggressive auditing in prior years by Business Tax section staff had effectively identified unregistered businesses that owed taxes. This effort has yielded, on average, over $1 million annually in past years.

We have examined a great deal of information in this section. Taking all of it into account, we are pessimistic that there is a sufficient number of unregistered businesses owing over $2,500 in tax to generate as much as $14.3 million dollars in additional Business and Payroll tax.[1]

---

[1] The 1993 Payroll Data provided by ED&R, adjusted for exempt employees was $12.30 billion and approximately $12.06 billion is on our BTS database for the same year, a difference of $240 million in Payroll expense or $3,600,000 in tax.

SECTION III.4: Taxicab Drivers

The Tax Collector recognizes the need to provide guidelines regarding the classification of taxicab drivers and this effort has begun.

The Tax Collector, in consultation with the state, decided to follow the State Employment Development Department's lead in determining taxicab companies as employers. Meanwhile, the Tax Collector has sought the City Attorney's opinion on the enforceability of such a determination. The City Attorney, citing *S.G. Borello & Sons, Inc. v. Department of Industrial Relations, (1989) 2 Cal.3d 341, 351*, stated that many factors that go into such determination and their weight changes from situation to situation. As a consequence, there is no easy way to make this determination.

The City Attorney advises that this office will need to undertake a detailed study of contracts and other conditions of the taxicab industry. Contracts and conditions vary from company to company and from time to time, thus causing determinations to fluctuate significantly.

We can expect cab companies to protest vigorously the application of the tax when the determination is made that they are employers. We can further expect that they may attempt to make modifications to their contracts with the cab drivers in an effort to escape future tax liability, as happened after the decision in *Santa Cruz Transportation, Inc. v. Unemployment Insurance Appeals Board (1991) 235 Cal.App. 3rd 1363* when the Court of Appeals determined that the cab companies were employers for purposes of the unemployment tax.

The City Attorney recommends amending the payroll tax ordinance to presume that cab drivers are employees, to avoid the problems discussed above.

The Budget Analyst estimates that, depending on whether taxicab drivers are classified as independent contractors or as employees, the Tax Collector would realize additional revenue of $702,750 to $1,376,700. We disagree with this projection of additional revenues. Many of the cab drivers are part-time drivers and would not be subject to the $150 business tax registration but instead, to the lower $25 fee which is only one-sixth of that amount.[35] Without an amendment to the tax ordinance, the collection of payroll taxes from taxicab companies cannot be considered a matter of certainty and no hard numbers can be reliably projected.

SECTION IV. 1: Delinquent Collections Process: Business Tax

The determination process referred to in the Budget Analyst's report is a function of: (1) the business tax ordinance (Sec. 1011) which allows the Tax Collector to estimate the amount of tax if a person fails to file a return, and (2) the small business exemption (Sec. 1005.3) granting businesses with a tax due of less than $2,500 to be exempt from tax. This practice of sending determinations based on available information or an arbitrary amount when such information is not available, is not unique to San Francisco;[36] other taxing jurisdictions and entities also estimate the amount of tax that may be owed, based on historical data and assumptions. What is made complicated in San Francisco is the small business exemption threshold of $2,500, which effectively required computed tax due of less than $2,500 to be raised to more than $2,500.

The Tax Collector recognized that the non-filer process for Business and Payroll Tax determinations was onerous and made somewhat unrealistic by the Small Business Exemption. To rectify this problem, the Tax Collector proposed an ordinance eliminating the Small Business Exemption for those businesses that fail to comply by filing the required annual statement. The Board of Supervisors approved this change in October, 1994 (File 127-94-10).

This will allow us, starting in Tax Year 1995, to make realistic determinations for non-filers as suggested in the audit report.

The matter of penalties is a somewhat more difficult issue. Municipal Code Section 909 (Payroll Expense Tax) and 1009.1 (Business Tax) allow a penalty for failure to file an annual registration certificate, failure to respond with financial information, or failure to file an annual tax statement, in the amount of <u>$100 for each tax year</u> if one or more of these three situations occurs.

The former Tax Collector, with advice of legal counsel, interpreted this to mean that the penalty should only be applied once, since most of the taxpayers who were not in compliance failed all three. My recollection is that he came to this decision because most of the non-filers were small businesses. The current Tax Collector is not opposed to changing this policy, but believes that since the penalty is now $500, the issue should be clarified legislatively as suggested by the Budget Analyst.

With the introduction of scanners to process Business/Payroll Tax Statements, the legislation to make realistic determinations, and the consolidation of our accounting process, we are now in a position to streamline our Business Tax collection process. With a delinquency date of February 28, mailing a first notice of delinquency in April -- though desirable -- may be too optimistic, given current resources.

The Budget Analyst states that the Business Tax section does not forward delinquent business tax accounts to the Investigations section until over one year after the accounts become delinquent. This finding is based on the Budget Analyst's selective review of known problem cases which do not reflect the typical time frame of 30-60 days. The cases selected for review by the Budget Analyst were delayed due to extraneous circumstances and were isolated cases.[37]

SECTION IV. 2: Consolidated Collections Process

We agree that it is desirable to pursue collections in the most efficient manner possible and are aware of the revenue potential and cost savings of being able to produce a consolidated delinquent tax statement for a taxpayer.

The Bureau of Delinquent Revenue has been pursuing development of the Columbia Ultimate Business System (CUBS), an automated collection system, for the past six years. This would consolidate, not only patient accounts, but also various taxes and licenses. The Columbia Ultimate Business System (CUBS) was approved in the FY 94-95 budget and is scheduled for installation on May 1, 1995.

The Business Tax System (BTS) currently consolidates all Business Taxes. Until a common taxpayer identification number can be obtained, the various Business Taxes and the personal property taxes will have to be manually consolidated on the CUBS system.

Three new collection officers have been hired to pursue unregistered businesses.[38] They are also being trained in the Business Tax process and will have access to the system for the in-house collection of Business Tax and Unsecured Personal Property Taxes. As the Tax Collector's on-going Total Quality Management (TQM) teams plan and implement a centralized accounting and taxpayer service unit, additional personnel will be trained in the use of the system.

While the Tax Collector has yet to establish an "automated" prioritization system, the Bureau of Delinquent Revenue, the Investigations and Legal sections do have priorities in which they pursue delinquencies. The Bureau of Delinquent Revenue has formalized procedures in the collection manual. We agree that vigorous pursuit of delinquent accounts can have a positive effect on voluntary compliance in the future.

The Investigations section has set the collection of Unsecured Personal Property Taxes as their collection priority for the past five years. Although a labor intensive process, collections have increased from $6,195,224 in 1990 to $10,801,747 in 1994. For the first nine months of this fiscal year, collections total $10,831,135. The Clearance Unit of the Investigations section, which was set up in 1989, collected over $2 million last year, which was mostly Business Tax money.

Legal section also operates under established priorities which include trust fund accounts such as parking and hotel taxes, and audit deficiencies. This is because of the three year statute of limitations and requirements for mandatory legal representations where failure to act would render accounts uncollectible. Representations include rejection of creditor claims in probates and bankruptcies, foreclosures and other related real estate litigation. These established priorities are based on the amount of resources available to the Tax Collector and City and County of San Francisco's budget priorities. However, with the

implementation of CUBS, we will also establish an automated prioritization system for Bureau of Delinquent Revenue and the Investigations section.[39]

The audit states that the Tax Collector does not perform simple, routine collections activities such as mailing delinquency notices. The Bureau of Delinquent Revenue sends over 22,000 automated notices per month. At least two notices are mailed for each delinquent tax bill before the investigators go into the field for in-person visits.[40]

Another serious concern is the suggestion by the Budget Analyst that we combine the Bureau of Delinquent Revenue, Investigations, and Legal into one section. This would be a major change in our operating structure that, we feel, needs further study. At present we are persuaded that the legal section needs to be a separate, independent entity reporting to the Deputy Tax Collector and the Tax Collector.[41]

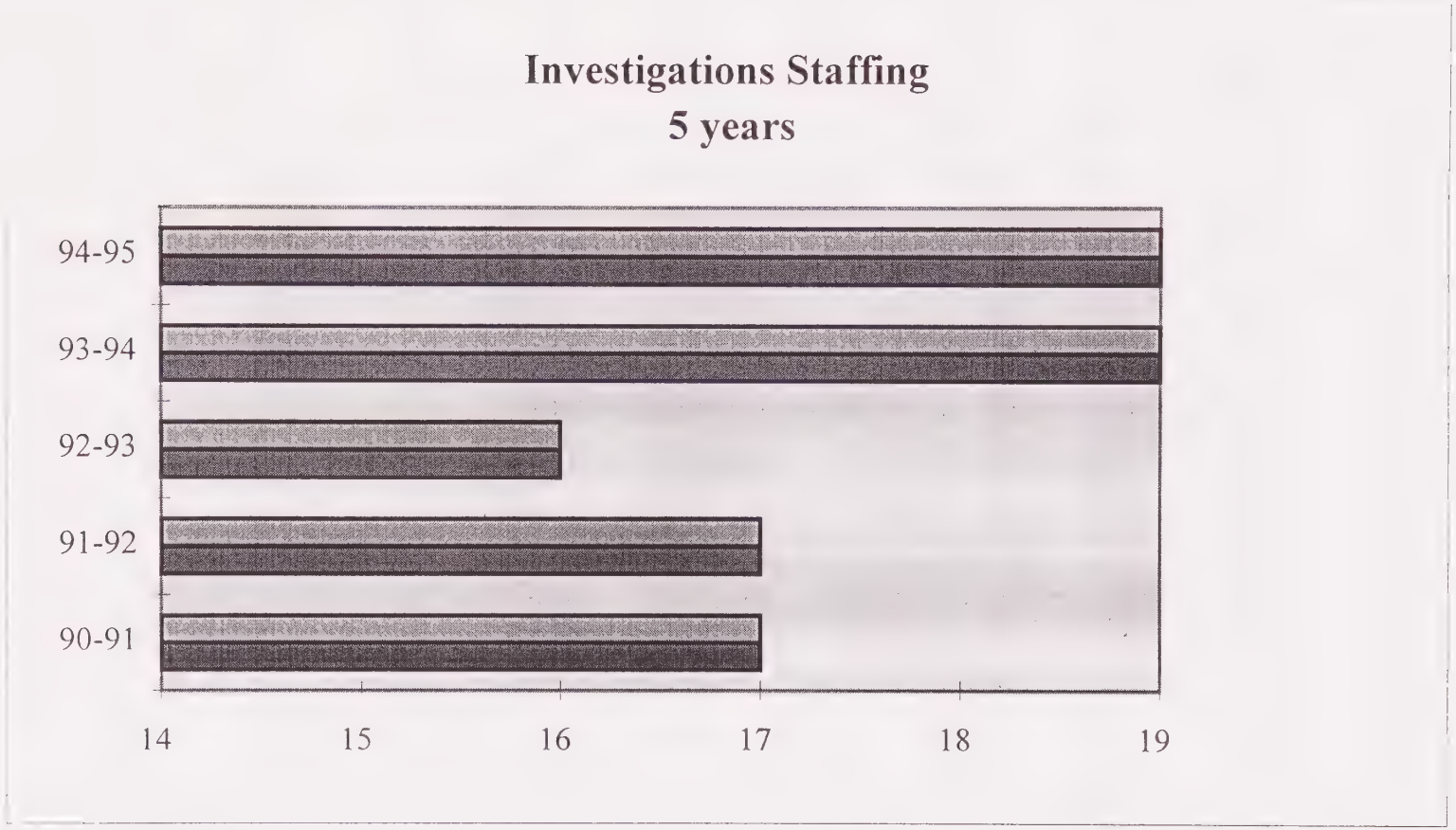

Investigations Staffing
5 years
94-95
93-94
92-93
91-92
90-91
14
15
16
17
18
19

Exhibit 1

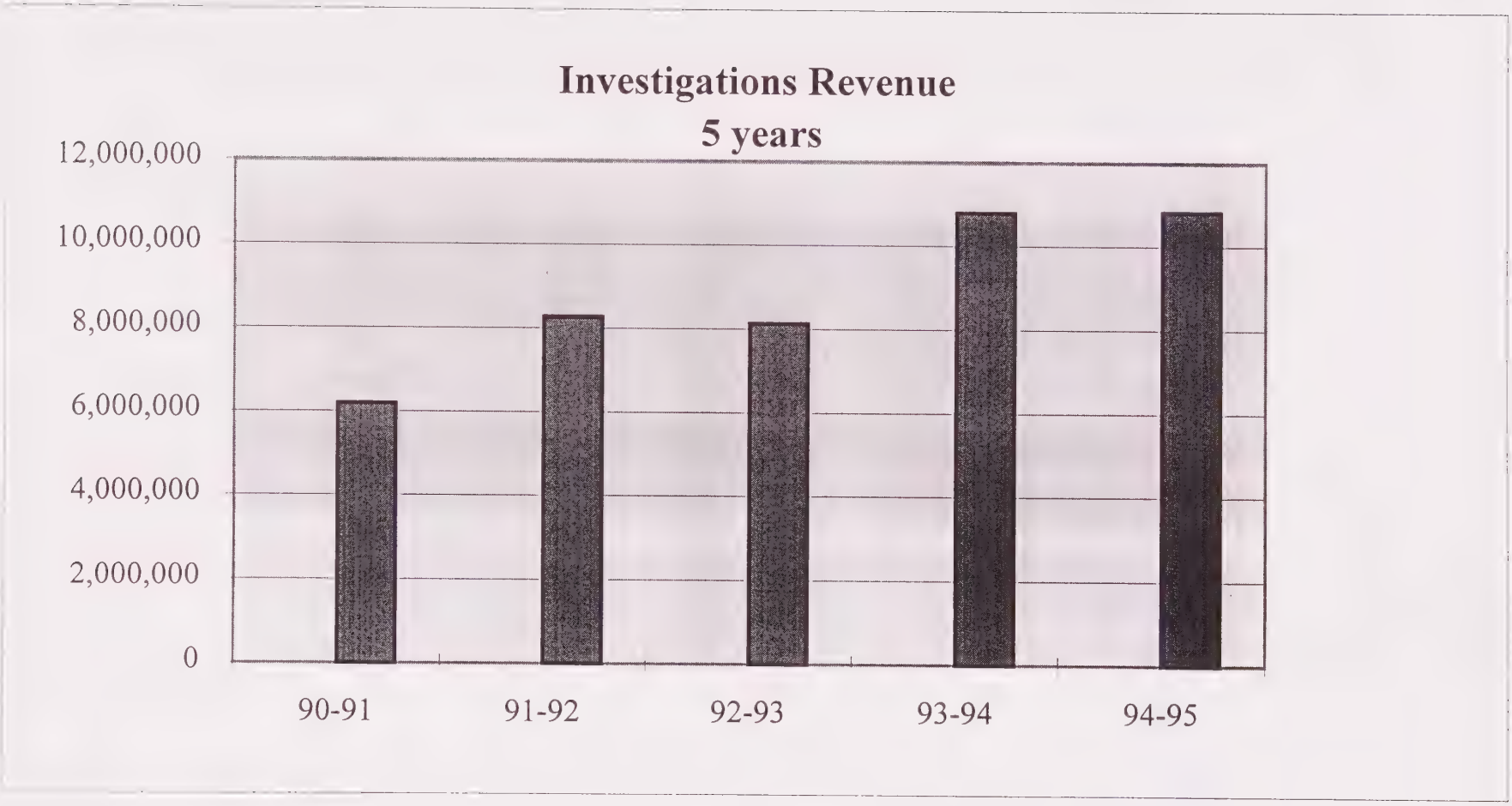

Investigations Revenue
5 years
12,000,000
10,000,000
8,000,000
6,000,000
4,000,000
2,000,000
0
90-91
91-92
92-93
93-94
94-95

Exhibit 2

Treasurer/Tax Collector Department
Ten Year Budget Comparison

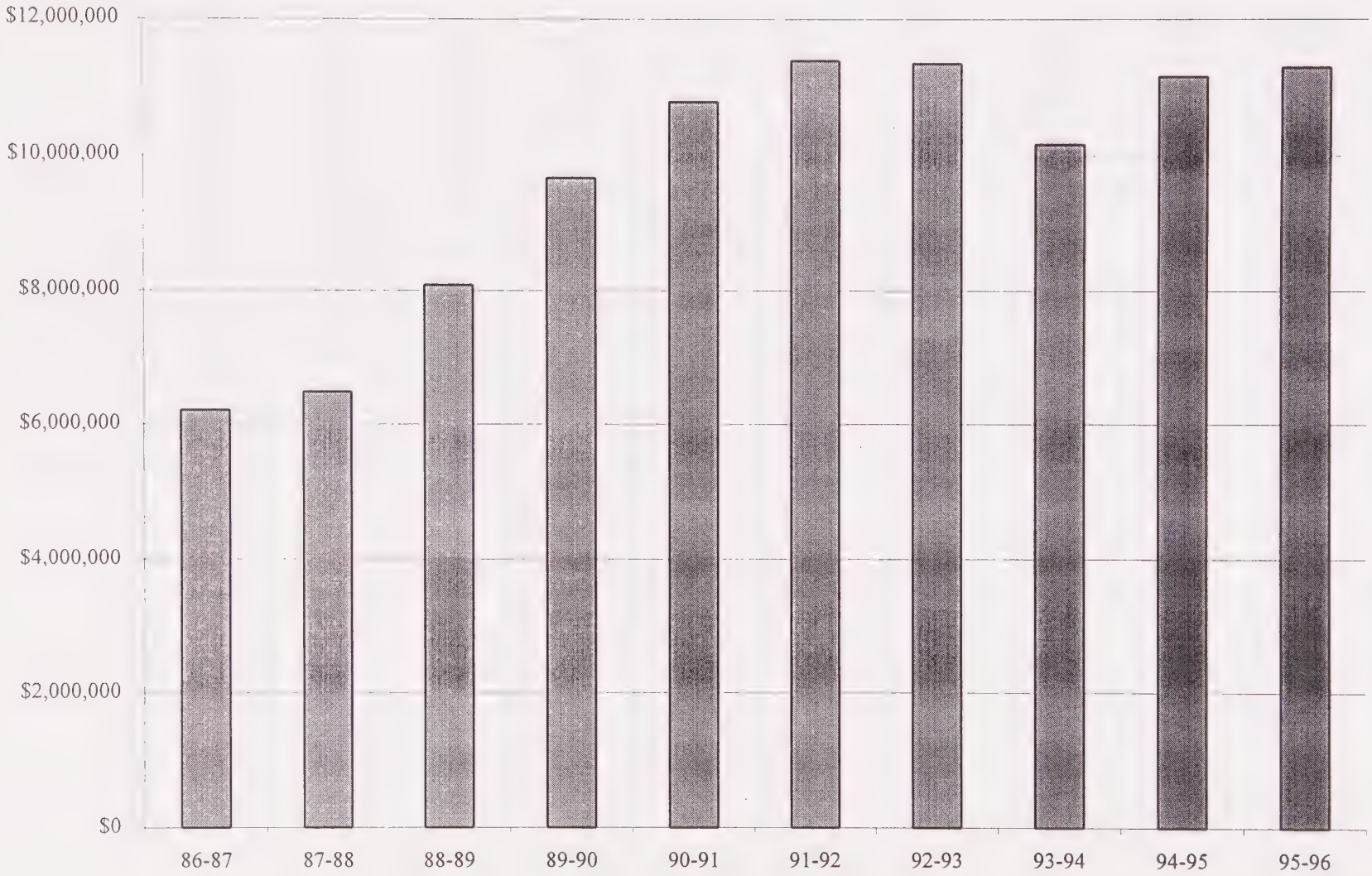


Exhibit 3

Treasurer/Tax Collector Department
Ten Year Revenue Comparison

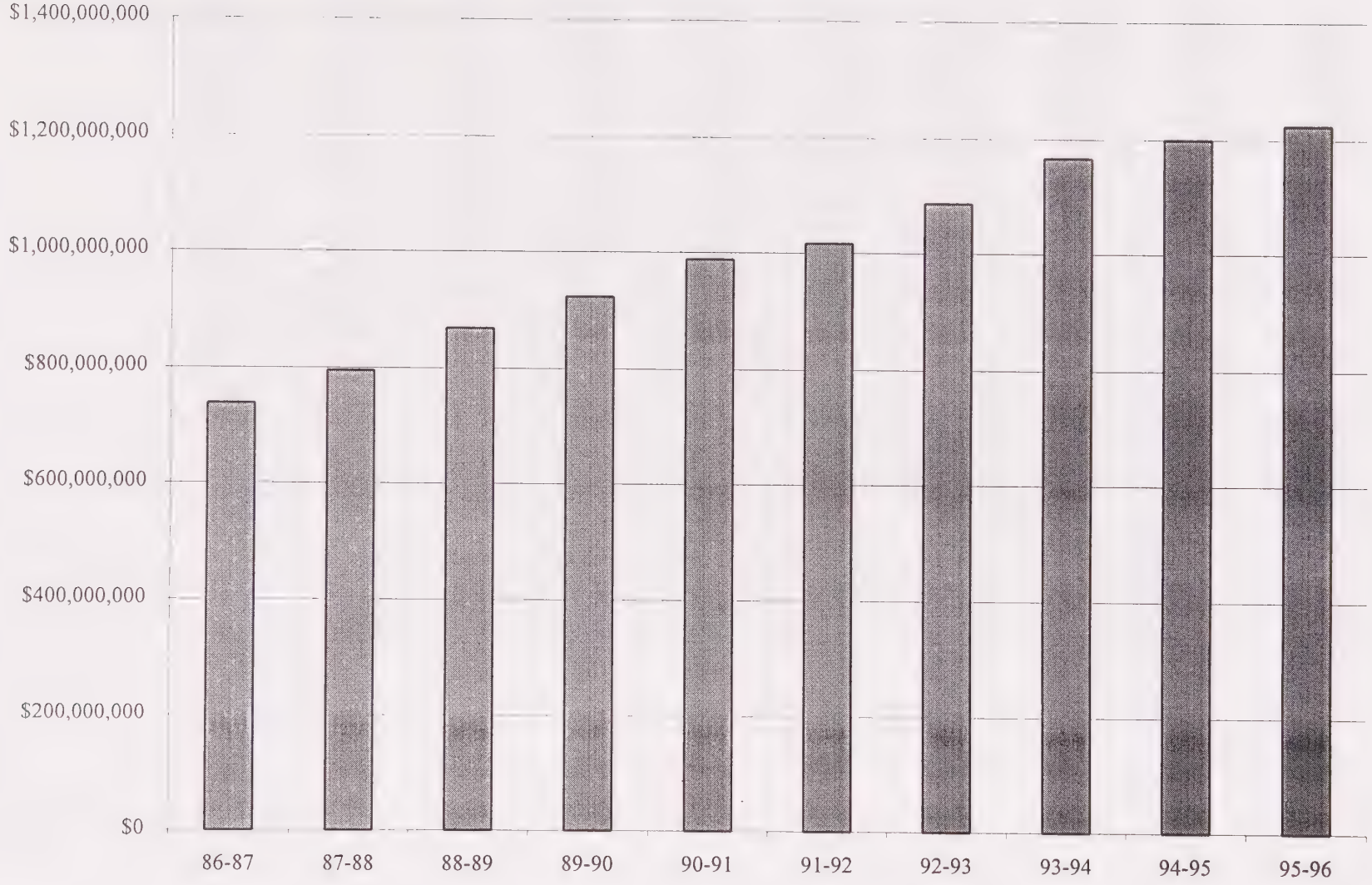


Exhibit 4


Treasurer/Tax Collector Department
Ten Year Staff Comparison
Staff
200
180
160
140
120
100
80
60
40
20
0
145
144
161
175
168
167
160
146
155
155
86-87
87-88
88-89
89-90
90-91
91-92
92-93
93-94
94-95
95-96

Exhibit 5

Treasurer/Tax Collector Department

Ten Year Statistical Comparison

	86-87	87-88	88-89	89-90	90-91	91-92	92-93	93-94	94-95	95-96
Staff	145	144	161	175	168	167	160	146	155	155
Budget	$6,213,684	$6,482,503	$8,084,235	$9,675,689	$10,790,552	$11,396,446	$11,353,952	$10,164,711	$11,164,553	$11,301,804
Revenue	$738,819,681	$795,914,640	$869,239,336	$923,418,044	$988,354,583	$1,016,833,645	$1,087,103,820	$1,167,731,863	$1,200,000,000	$1,224,000,000

Exhibit 6

BUDGET ANALYST'S REBUTTAL TO TAX COLLECTOR RESPONSE

The following are the Budget Analyst's rebuttals to the Tax Collector's response to our 1995 management audit of the Tax Collector's Office. We have inserted numbers in the Tax Collector's response to correspond with our numbered rebuttals, below.

INTRODUCTION

1. None of the recommendations contained in this report pertain to property taxes, which represent approximately 65 percent of the Tax Collector's total collections. Our recommendations represent 6 to 8.5 percent of non-property tax collections.

SECTION I.2: AUTOMATION

2. This quote is taken out of context. Our point, as stated on page 33, is that the $3.75 million investment in new automated systems is "largely going to waste, because staff have not been trained to take advantage of the improvements."

3. All information relevant to the taxpayer is not in one place: Unsecured Personal Property taxes and licenses are maintained in separate systems.

4. The Office of the Controller stated in an April 7, 1995 memo to the Budget Analyst that "The denial of access to certain screens even to certain Tax Office personnel, is a manifestation of the Tax Collector's well known philosophy of maintaining tight system security and control. This will at times result in inefficiencies (and staff frustrations) which arise from separation of duties/responsibilities. It is also possible that security and control has been taken a tad too far."

5. Our final report does not state that end-users of custom software have no effective input into the design, installation, or modification of custom software, although we did find certain examples where employee input could have been improved.

SECTION I.3: TAXPAYER ASSISTANCE

6. So noted.

SECTION II.1: LICENSING

7. The implementation target of FY 1996-97 was suggested by the Tax Collector's Office.

8. Our report notes that legislative changes must be identified and implemented prior to consolidating licenses with property tax and business registration billings.

9. One-time scheduling modifications should not deter the Tax Collector from making efficiency improvements.

10. Based on interviews with user departments, user departments are currently dissatisfied with the Tax Collector's performance in collecting license revenues. User departments were generally supportive of consolidation efforts, and no user departments expressed trepidation about this consolidation proposal.

11. Again, the one-year implementation schedule was suggested by the Tax Collector's Office.

12. Although individuals often respond negatively to change, we do not concur that additional fees attached to the property tax bill will result in lower compliance, since: (a) license fees are insubstantial relative to the property tax and special assessment fees already included on the property tax bill; (b) consolidation will not result in any overall increase in license fees, and such fees must be paid annually, regardless of the payment due dates; and (c) overall property tax collection is virtually 100 percent, since the Tax Collector can seize and sell property to collect payment.

13. Our report states that "An amendment to the Annual Salary Ordinance to eliminate ... existing positions is a policy decision, based on whether (1) the Tax Collector's justification for the use of these positions in other Divisions; and (2) the Board of Supervisors prefers that such reductions be accomplished through attrition."

14. The 90.1 percent collection rate for DPW and Rent Board fees on page 68 of our report reflects written information provided by the Tax Collector's Office.

SECTION II.2: DOG LICENSES

15. As noted in footnote 2 of this section, "This estimate is based on national statistics prepared by the Society for the Prevention of Cruelty to Animals (SPCA) indicating that 37 percent of households have dogs, and each of these households has 1.5 dogs on average. San Francisco had 319,000 households in CY 1992. However, San Francisco's dog population may be lower than the national average, due to the high proportion of rental property."

SECTION III.2: REVIEW OF CITY PARK AUDIT

16. The Tax Collector's audit of City Park included calendar years 1991, 1992, and 1993. The DPW's 1985 traffic flow study was therefore conducted six years prior to the first audit year. Also, as noted in our report, in 1990 the DPW performed an actual count of the number of passengers in 200

automobiles entering the parking lot, which showed an even lower average than the 1985 traffic flow study.

17. These points are not relevant to our finding.

18. One of our major disagreements with the Tax Collector's methodology is that it considers only one day. This point underscores our finding that the DPW's method, which evaluated more than one day, is superior.

19. These points are addressed in our report.

20. In response to repeated requests from the Budget Analyst's Office, the Tax Collector provided a set of working papers, which we reviewed. If these working papers were incomplete, that is the responsibility of the Tax Collector. Furthermore, the fact that we were unable to ascertain that the working papers were incomplete supports our contention that such papers were not sufficiently annotated.

21. Our review of the Tax Collector's working papers indicated that the audit team "neglected to assemble the complete working papers necessary to establish an audit trail, to permit thorough supervision by senior staff auditors and to permit review by any experienced auditor." We stand by these findings.

22. Again, omissions in the working papers are the responsibility of the Tax Collector's Office.

SECTION III.3: BUSINESS REGISTRATION

23. A random sample could not be completed, because in order to perform scientific sampling, an accurate list of the population (in this case, San Francisco businesses) must be available. The fact that no accurate list of the population of San Francisco businesses exists is exactly the problem addressed in this section of our report.

24. It is just as likely that our estimates are understated.

25. We present various estimators that show a range of estimated number of businesses.

26. This Employment Development Department (EDD) estimate grossly understates the number of businesses in San Francisco, since EDD only retains records of businesses with employees. The fact that the Tax Collector has included this obvious underestimate, which lists less than half as many businesses as the number actually registered by the Tax Collector, causes the Budget Analyst to question whether the Tax Collector intends to represent or understate the actual number of businesses in San Francisco in his response.

27. The Tax Collector's survey cannot be random, because no accurate list of the population of San Francisco businesses exists.

28. We take strong issue with the Tax Collector's contention that his survey is more representative than the Budget Analyst's survey. The Tax Collector selected only businesses in San Francisco's financial district, where businesses are likely to be more stable and larger, and the types of businesses are limited. Our survey included several locations and a variety of businesses, including commercial, retail, manufacturing, and service industries.

29. We identified several problems with this methodology of the Tax Collector's Office, which are detailed in our report. Most notably, the Tax Collector's methodology does not identify sublessors. The methodology we used to estimate the number of unregistered businesses corrects for the weaknesses in the Tax Collector's methods.

30. It is important to note that: (a) the Tax Collector's budget justification for these positions does not specify that these positions will be dedicated to identifying unregistered businesses; (b) these three positions have been assigned to the Amnesty Program, and have spent no time identifying unregistered businesses; and (c) the Tax Collector and the Investigations Division Manager are not in agreement as to the anticipated activities of these employees, based on a telephone interview with the Investigations Division Manager of April 17, 1995.

31. If the Investigations Division is responsible for identifying and registering unregistered businesses and for conducting periodic surveys in search of unregistered businesses: (a) these activities are not being performed; and (b) Tax Collector personnel does not generally understand this allocation of responsibilities, since we interviewed numerous staff persons with varying levels of responsibilities, from Division Managers to line staff, who did not understand that the onus of responsibility for business identification was centered with the Investigations Division.

32. We found the Clearance Unit to be very effective, and hope that it is not merely a temporary creation.

33. As noted in Section III.1 of this report, Business Tax Auditing, we do not consider the identification of delinquent business registration fees and business taxes to be an effective use of auditor time. Pursuit of delinquent fees and taxes should more appropriately be conducted by collections personnel.

34. As noted in our report, this $14.3 million may understate the amount of businesses taxes that may be generated, because it is based on the smallest estimate of unregistered businesses in San Francisco. Using our highest estimate of the number of unregistered businesses, we state that a maximum of $81.3 million could be generated from unregistered businesses.

SECTION III.4: TAXICAB DRIVER STATUS

35. Any business earning over $15,000 annually must pay at least $150 in annual registration fees. As noted in footnote 2 of this section, "According to the *American Almanac of Jobs and Salaries*, the 1991 median salary for taxicab drivers was $17,628. Based on average annual inflation of two percent, the 1995 median salary for taxicab drivers would be $19,463. We have inflated the salary 2.8 percent, because the total median salary in San Francisco is higher than average, according to the 1990 United States Census." However, we acknowledge that some taxicab drivers likely earn less than this amount.

SECTION IV.1: DELINQUENT COLLECTIONS PROCESS: BUSINESS TAX

36. As noted in our report, certain cities, including Los Angeles, estimate business taxes for businesses that do not file based on realistic assumptions for the type, size, and location of the business, not at a flat 150 percent increase over the previous tax year, as San Francisco does.

37. The Budget Analyst did not conduct a selective review of isolated cases in this circumstance, but rather this analysis was based on a comprehensive review of all delinquent business taxes.

SECTION IV.2: CONSOLIDATED COLLECTIONS PROCESS

38. See number 31, above.

39. In response to this and the previous two paragraphs, we did not state that the individual divisions have not established collection priorities. We state that the Tax Collector's Office has not established uniform, multi-variable priorities that will maximize collections of delinquent revenue overall.

40. Our report acknowledges that the Bureau of Delinquent Revenue (BDR) mails automated letters. This practice should be implemented consistently for all delinquent revenue collections, as noted in our report.

41. We see no compelling reason to maintain a separate Legal Division, since the Tax Collector Attorney's <u>only</u> allowable responsibility under the Charter is delinquent revenue collection. In contrast, we see reason to consolidate the Legal Division with BDR and the Investigations Division, since our proposed consolidation would: (a) establish legal oversight for small claims and bankruptcy charges; and (b) allow the consolidated Collections Division to consider legal collections issues in establishing its prioritization system.

Appendix A
Police Department Licenses for Individuals Versus Businesses

Licenses for Individuals

Taxicab
Taxicab - Paratransit
Jitney Bus Driver
Escort Service (Employee)
Masseur or Masseuse Trainee
Peddler Employee
Tow Car Driver
Pedicab Operator
Encounter Studio (Employee)
Nude Model-Public Photography (Employee)

Licenses for Businesses

Mechanical Amusement Device
Amusement Park
Driverless Auto Rental
Licensed Tour Guide
Mechanical Contrivance
Museum
Photographer - Public Place
Photographic Solicitor
Street Photographer
Shooting Gallery
Skating Rink
Billiard Parlor
Photographer - Public Place
Junk Dealer
Street Photographer
Limousine
Photographic Solicitor
Auto Wrecker
Public Bathhouse
Cabaret
Dance Hall Keeper
Place of Entertainment
Junk Gatherer
Pawnbroker

Massage Establishment
Bingo Games
Mobile Caterer
Peddler, Food
Peddler, Non-Food
Pedicab Owner
Jitney Bus Owner
Escort Service (Owner)
Assistant Mobile Caterer
Masseur
Masseuse
Junk Gatherer
Dirver Public Passenger Vehicle
Outcall Massage Service
Pushcart Peddler
Valet Parking - Fixed Location
Valet Parking - Annual Special Event
Secondhand Dealer/Antique Shop
Secondhand Dealer
Ball or Ring Throwing Games
Advertising Distributor (Class A)
Advertising Distributor (Class B)
Encounter Studio (Owner)
Funeral Procession Escort
General Soliciting Agent
Interurban/Sightseeing Bus
Commercial Loudspeaker
Miniature Golf Course
Motorized Rickshaw
Nude Model-Public Photography (Owner)
Vehicle for Hire, Non-Motorized
Charitable Promoter
Poker
Public Outcry Sales
Recreational Equipment Vendor
Taxicab Radio Dispatch Service
Trade-in Dealer
Dealer in Firearms and Ammunition
Balloon and Kite Advertising
Discharge of Cannon
Circus
Circus (located at Civic Center)
Itinerant Show (Per concession)
Masked Ball
Off-Heliport Landing Site
Rodeo Exhibition/Wild West Show

Appendix B

Detailed Explanation of Consolidated Collections Flow Chart

Delinquent Accounts Section receives delinquent accounts information.

In Section I.1 of this report, we recommend that the Tax Collector centralize accounting functions under an Accounts Services Division. This Accounts Services Division would include a Delinquent Accounts Section responsible for issuing consolidated delinquent accounts statements and mailing these statements and collection letters to delinquent accountholders. The Delinquent Accounts Section would receive the delinquent account information from the Property Tax Division, the Business Tax Division, or from another Section of the Accounts Services Division, depending on which Division(s) are responsible for regular billing activities.

Delinquent Accounts Section identifies all other fees and taxes due

The Delinquent Accounts Section would compile a consolidated statement detailing all outstanding revenues owed by an accountholder, including standardized fees and penalties. The thrust of this activity would be delinquent revenues owed by businesses, i.e., delinquent UPP taxes, business taxes (i.e., payroll and gross receipts taxes parking taxes, hotel taxes, utility user's taxes, etc.), business licenses, and business registration fees.

Ideally, the consolidated account information should be retained in a database that automatically updates interest and penalties. Personnel in the Collections Division should have read-only access to this database, and should use <u>only</u> this database in determining the amount of outstanding delinquent revenue. At the same time, the Tax Collector's other databases (such as the Business Tax System) should be modified so as to make <u>no</u> interest calculations, and the Delinquent Accounts Section of the Accounting Division should be the only location in the Tax Collector's Office that determines total outstanding revenue. Having only one database perform penalty and interest calculations would eliminate disagreement from Division to Division regarding the actual amount owed by a taxpayer.

In Section I.2 of this report, we recommend that the Tax Collector consolidate his databases. Establishing a consolidated database would minimize or even obviate the need for the Delinquent Accounts Section to prepare a consolidated statement, since consolidated information would be readily available. However, due to the length of time it may take to fully consolidate these databases, the Delinquent Accounts Section is a necessary interim measure. After the consolidated database is in place,

there would certainly be no need to retain a separate database listing the consolidated delinquent accounts.

Delinquent Accounts Section sends automated letter first day and after 30 days

The Delinquent Accounts Section would send an automated letter as soon as the consolidated statement is complete. This automated letter would inform the delinquent accountholder that all outstanding taxes, fees, penalties and interest must be paid immediately, or further action will be taken. If the account is not paid in full as a result of this letter, a second letter would be mailed, approximately 30 days after the first mailing, stating the Tax Collector's intent to seize and/or lien the delinquent accountholder's property.

If the delinquent accountholder requires a business license or registration, this license or registration should be withheld until the account is paid in full. According to the GAO survey, states found that suspending a taxpayer's business and professional licenses and permits if the delinquencies remain unresolved is an effective means to collect delinquent revenue. According to the 43 states that responded to the GAO survey, updated written billing procedures and use of enforcement programs that restrict taxpayer access to certain state licenses and permits increase collection efficiency.

Accounting Section refers to Collections Division

In cases where the account is not paid in full (and thus closed), the account is above the minimum dollar amount, and a checking account has been identified, the Delinquent Accounts Section would refer the account to the Collections Division. The minimum dollar amount is a policy decision that will impact the Tax Collector's resource requirements. The lower the dollar amount, the more resources the Tax Collector will require, since a collection agency will collect on all accounts below the minimum, and the Tax Collector will collect on all accounts above it. (Currently, the Investigations Division attempts collections and places liens on UPP accounts of $20 or more, while BDR refers accounts of less than $2,500 to a collection agency after three notifications. This wide discrepancy argues for a standard minimum amount for pursuit by the Investigations Division versus referral to a tax collection agency.)

Seizure Unit seizes checking account

As indicated on the above organization chart, the consolidated Collections Division would include a Seizure Unit. The State Revenue and Taxation Code empowers the Tax Collector to seize and sell a delinquent taxpayer's personal property, improvements, or possessory interest. This power is not limited to seizure of only the personal property being assessed.[1]

---

[1]There is a three year statute of limitations on the lien date for such seizure and sale.

The seizure of financial assets, particularly checking accounts, would be the first step after sending several letters requesting compliance, because such seizure is a largely administrative process that would eliminate the need for extensive in-person or other collections activities: seizing checking accounts is non-labor intensive and usually gets results. Investigators in the Seizure Unit would attempt to locate checking account information using prior payments and bank location, and would directly notify identified banks of intent to lien. Delinquent accountholders' checking accounts would be frozen pending an administrative hearing; after the administrative hearing, the bank would remit funds directly to the Tax Collector. The Tax Collector's administrative costs to seize such financial assets could be assessed to the delinquent taxpayer.

Based on the Budget Analyst's telephone survey, the Counties of San Mateo, Marin, Santa Clara, Los Angeles, Orange and San Diego use the seizure of checking accounts to enforce the collection of delinquent revenues. In fact, San Mateo County has worked cooperatively with Marin County to enforce the collection of delinquent UPP Taxes for businesses that move from one County to the other. These counties include the administrative costs associated with such seizures in the total amount to be paid by the delinquent taxpayer.

Such seizure procedures could be implemented immediately for Unsecured Personal Property (UPP) Tax delinquencies, since UPP is governed by the State's Revenue and Taxation Code. However, in order to implement this step for business taxes, as noted above, the Board of Supervisors would need to approve an ordinance authorizing the Tax Collector to seize and sell property in accordance with State law.

Lien placed automatically

If the delinquent account is not paid in full as a result of seizing the checking account, a lien would be automatically placed on the individual, business, and/or property of the delinquent accountholder. The Tax Collector does not have the resources to seize and sell property other than real property; however, future revenue might result if any licensed business or property changes ownership. Such a lien could remain in place for 30 years.

Priority System

The Tax Collector and the Collections Division manager should establish a prioritization system for the collection of delinquent revenue to determine the treatment of accounts. This prioritization system should include collectability, amount, and time limitations, and should be automated. Whenever the Collections Division receives a delinquent account, and whenever an account is paid in part, that account should be prioritized using this automated system. Accounts should be divided into "High" and "Low" priority; high priority accounts should be ranked from highest to lowest priority; low priority accounts, which would either be classified as inactive or referred to a collection agency (see below), do not need to be ranked.

Although not noted on the above flow chart, the Division Manager (or his designee) should conduct a cursory reasonableness check on all low priority accounts. Any accounts that seem out of place as a low priority, such as accounts with a high dollar amount, should be removed and reviewed more closely. We recommend this reasonableness check because low priority accounts would not otherwise be seen by human eyes.

Account assigned to Investigator

High priority accounts should be assigned to Investigators. If an Investigator disagrees with the High Priority designation, the account should be brought to the attention of the Division Manager for review.

Investigator pursues account in priority order

Investigators should pursue the accounts in order of priority. Investigators should attempt telephone collections first; if a partial payment is received, the account should be reprioritized. If no payment is received, the Investigator could pursue in-person collections, but only for those accounts of the highest priority. (According to the 43 states that responded to the GAO survey, increased use of telephone collection techniques increases collection efficiency.) If a partial payment is received as a result of in-person collections, the account should be reprioritized.

The City of San Jose and the City of Oakland have Peace Officers performing in-person collections. These Peace Officers issue citations requiring the delinquent business owner to appear at a Superior Court hearing. If the owner does not appear, a warrant is issued for his or her arrest. If the owner appears but does not pay a fine, the Superior Court Judge may declare him or her to be in contempt of court, and imprison them. According to the City of Oakland, issuing such citations has been a very effective means to collect delinquent tax revenues, and no business owner has ever been jailed. Peace Officers' annual salary and benefits are higher than Investigator's salary and benefits. The Board of Supervisors and the Tax Collector should consider replacing one or two Investigators with Peace Officers, since Peace Officers if necessary, are authorized to cite individuals and require them to appear in Superior Court.

Investigator refers account to Legal Section

If Investigators' activities do not result in payment or in partial payment where the account is still considered high priority, the account should be referred to the Legal Section. As noted on the above organization chart, the Legal Section would be responsible for small claims and bankruptcy proceedings, as well as for major claims. Small claims and bankruptcy proceedings would be implemented by a staff of non-lawyers. Although this does not appear on the above flow chart, bankruptcy personnel should continue present activities of identifying bankrupt businesses and matching them with delinquent accounts. If a delinquent accountholder is identified as bankrupt, that account should be moved immediately to the Legal Section.

Legal Priorities

The Legal Section, which would include a small claims function as well as an attorney function, should apply the same prioritization system to delinquent accounts. High priority accounts should be pursued through the courts. Low priority accounts should become inactive, or should be referred to a collection agency, if such a referral is legal.

Refer account to collection agency

Low priority accounts are referred to a collection agency (except for UPP accounts) because a collection agency charges fees based on a percent of revenue collected. Therefore, even if the Tax Collector himself does not pursue an account because it is low priority, the Tax Collector may recover a portion of the debt through a collection agency. UPP accounts may not be collected by a collection agency, according to the State Revenue and Taxation Code.

Account becomes inactive

An account becomes inactive only if it is a UPP account and if it is classified as low priority using the prioritization system described above or if it is less than $20. Very low priority accounts should be classified as inactive so that the Tax Collector may focus resources on accounts that will likely result in greater revenue.

Sue or Settle

High priority accounts in the Legal Section would result in suing or settlement. Low priority accounts would be referred to a collection agency, or become inactive.

Account paid and closed

A delinquent account could be paid in full at any point in the process and closed.